

CHAPTER 6

JAPAN'S ECONOMIC WOES AND AUSTRALIA'S PROSPECTS

Introduction

6.1 Having briefly traced the evolution of Australia's trading links with Japan from the 1860s to 1990 when Japan's bubble economy collapsed, the Committee now turns to recent developments in the Japan-Australia trading relationship. The Committee draws on specific sectors within the Australian economy to provide an understanding of how Japan's domestic circumstances and economic troubles have influenced Australia's economic prospects. It also addresses the growing complexity and diversity in Australia's trading relationship with Japan and considers current and potential difficulties in that relationship.

Statistical overview of Australia's trade with Japan from 1990

Share of Australia's export market

6.2 Japan has been Australia's most significant trading partner since 1967. During the mid-1970s, Japan was vital to Australia's economic interests with over 30% of all Australian exports going to Japan. Although its dominant share of Australia's total exports has gradually slipped back, Japan at the beginning of 1990 held its position as Australia's principal export destination and second largest import supplier. It accounted for a substantial 26% of Australia's exports and 19% of imports.¹

6.3 Clearly, over the years, Australia had become heavily reliant on Japan as an export market, especially for key Australian exports such as coal, iron ore, wheat and beef. The unprecedented growth in the tourist industry, which by 1990 was making a major contribution to national economic development, was due in part to the increasing number of Japanese visitors who, by this time, were the single most important tourist group to Australia. By 1990, they made up 21.7% of all overseas visitors to Australian shores.² Moreover, by 1990, Japanese investment in Australia was the third largest and almost matched that of the United States and the United

1 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile, International Accounts and Trade, Feature Article—Australia's Merchandise Trade with Japan', (March 1999) <http://www.abs.gov.au/Australia/websitedbs/c311/BDE7ACE2081C70E6CA25677B00077C49> (30 November 2000). The US is Australia's second most important trading partner, it takes around 19% of Australia's total exports and supplies Australia with over 20% of its imports.

2 By 1990, Japanese tourists had eclipsed the number of New Zealand visitors who made up 18.9% of the market; *Official Year Book of the Commonwealth of Australia*, no. 75—1992, p. 389.

Kingdom.³ So, at the beginning of the 1990s, Japan occupied a central position in Australia's trading interests. This close relationship meant that the effects from any major economic developments in Japan would flow through to the Australian economy and affect Australia's economic growth through its international trading activities.

6.4 Thus, when the Japanese economy started to slow in the early 1990s and edged toward recession in the latter half of the decade, most economic analysts expected Australia would suffer directly through its trade and financial linkages. They predicted that subdued economic activity in Japan would soften demand for Australian products and hence damage Australia's potential for economic and export growth.⁴

6.5 To some extent such expectations have been correct. Since 1990, when Japan entered a prolonged period of sluggish economic activity, its dominance as an export destination for Australian products and as a supplier of goods to Australia has been eroded. Even so, Australia's export trade to Japan has held up well to date and Japan still retains its position as Australia's single largest export market.⁵

6.6 Japan's share of Australia's total exports fell from 23% in 1995 to below 20% in 1996.⁶ In 1997, exports to Japan accounted for 19.8% of total exports. Australia's export growth to Japan slowed in 1998 and Japan's share of Australia's total export trade dipped slightly to 19.6%, falling to 19.2% in 1999.⁷

Japanese imports to Australia

6.7 The United States has been Australia's major source of imports for many years. After the United States, Japan is Australia's second largest source of overseas goods. In 1989, Japan held a 20% share of Australia's import market. Over the last decade, this share has declined to around 14%. Imports from Japan stood at \$A13.3 billion or 13.8% of total imports in 1998. This share of total imports slipped to 13.4%

3 The official figures produced by the Australian Bureau of Statistics show the following levels of investment in Australia for 1989–90 in \$ million: US—46,386; UK—46,092 and Japan—45,364, *Official Year Book of the Commonwealth of Australia*, no. 75—1992, p. 711.

4 DFAT, submission no. 32, pp. 64–5; NSW Government, submission no. 25, p. 10.

5 Barry Jones, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, pp. 690 and 695.

6 Trade Analysis Branch, Department of Foreign Affairs and Trade, June 1999, *Exports of Primary and Manufactured Products, Australia 1996*, Canberra, p. 12.

7 NSW Government, submission no. 25, p. 1; Market Information and Analysis Unit, Department of Foreign Affairs and Trade, *Composition of Trade Australia, 1998*, Canberra, p. 44; Trade Analysis Branch, Department of Foreign Affairs and Trade, *Exports of Primary and Manufactured Products Australia, 1997*, p. 7; Barry Jones, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, pp. 689–90; DFAT, submission no. 32, p. 33 (DFAT gave the figure of 19.5% of total exports for 1997 and 13% of total imports). Additional information supplied to the Committee by DFAT, 18 May 2000.

in 1999. Although Japan's share of Australia's market has fallen, it retains its position as Australia's second major source of imports. The United Kingdom holds third place, although its share of the Australian market has also declined over two decades from 11.5% to 6.2%. Countries such as China, the Republic of Korea and Indonesia have increased their share of the Australian market since 1977 by 4.8%, 3.1% and 2.4% respectively.⁸

6.8 The following table shows the gradual decline in Japan's share of Australian exports and the fall in Japan's share of total Australian imports since 1989.

Table 6.1—Australia's merchandise trade and trade share with Japan 1989–1998.

	Exports to Japan	Share of Australia's total exports	Imports from Japan	Share of Australia's total imports	Balance of trade with Japan
	\$m	%	\$m	%	\$m
1989	12,441	26	10,508	20	1,933
1990	13,441	26	9,358	19	4,083
1991	14,820	28	8,728	18	6,092
1992	14,749	25	10,037	18	4,712
1993	15,627	25	11,885	19	3,742
1994	15,993	25	12,100	18	3,893
1995	16,566	23	11,965	15	4,601
1996	15,565	20	10,213	13	5,352
1997	16,814	20 (19.8%)	11,409	14	5,405
1998	17,403	20 (19.6%)	13,319	14	4,084 ⁹

8 Market Information and Analysis Unit, Trade Development Branch, Department of Foreign Affairs and Trade, February 1999, *Australian Basic Trade Statistics 1997–98*.

9 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.Australia/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocument> (30 November 1999) (page 2 of 15).

Australia's share of the Japanese import market

6.9 Even though the growth in Australia's exports to Japan has continued to decline, Australia's share of the Japanese import market has increased marginally in the last few years. Australia's overall market share in Japan increased from 4.1% in 1996 to 4.3% in 1997, reversing a downward trend over recent years. Australia improved its ranking from being Japan's eleventh most important trading partner in 1997 to rating as seventh in 1998. In general, Australia performed better than its competitors in the Japanese market—it managed not only to maintain its share of a diminishing market but to increase this share slightly. Austrade pointed out that in 1998, Japan's global imports declined by 10.5% but Australian imports into Japan declined by only 3.6%.¹⁰ In 1999, however, Australia's share of Japan's import market fell back to its 1996 share of 4.1%.¹¹

6.10 Although the growth rate of Australian exports to Japan has slowed, the decline in Australian exports to Japan has not been severe. This is due in large measure to the depreciation of the Australian dollar against the United States dollar and against major European Union currencies.¹² Thus, according to DFAT, the concern that Australian trade with Japan would suffer has not been fully realised because the 'realistic' level of the Australian dollar largely cushioned Australian exporters, resulting in a rise in Australia's share of Japan's import market in 1998 with a slight fall in 1999.¹³

Economic slowdown in Japan and its effects on Australia

6.11 Although any negative effect on Australian trade stemming from reduced economic activity in Japan has been largely offset to date by the increased competitiveness of Australian exports resulting from, among other things, the depreciation of the Australian dollar, the fear lingers that any deepening or prolongation of the recession in Japan could further dampen Japan's demand for Australian products.¹⁴

6.12 The exchange rate that favoured Australian exports by giving them a competitive edge explains in part why Japanese demand for Australian goods did not fall away steeply. The trading relationship between Australia and Japan, however, is complex and there are many other factors at work that have helped buffer Australia

10 Greg Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 628; Colin Heseltine, DFAT, *Committee Hansard*, 15 February 1999, pp. 2–3; NSW Government, submission no. 25, p. 1.

11 Additional information supplied to the Committee by DFAT, 18 May 2000.

12 DFAT, submission no. 32, pp. 65–7; ABARE, submission no. 21, p. 10.

13 DFAT, submission no. 32, p. 65; Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 731.

14 Queensland Government, submission no. 18, p. 1; Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 731.

against the ill winds of Japan's economic troubles. The strong relationship between the two countries that spans many years and the reputation that Australia has built up as a reliable supplier and dependable trading partner provides a solid platform for future growth in the Australia-Japan relationship despite economic difficulties. Mr Fuyuki Kitahara, President of the Japanese Chamber of Commerce in Sydney, suggested:

Despite negative growth in Japan for the past two fiscal years, the impact on Australia in these key areas has not been negative to the extent that might have been expected. My personal view is that the comparatively small downwards movement is the direct reflection of the fact that Japan places a high priority on Australia in these areas based on quality, competitiveness and stability.¹⁵

6.13 Notwithstanding Australia's good name as a reliable and stable trading partner, slow economic growth in Japan will mean continuing weak demand for Australian goods, which will in turn exert downward pressure on both volume and prices. Exports likely to suffer from expected continuing low growth include Australia's rural commodities, especially wool, seafood, forest products and possibly cotton. According to the Australian Bureau of Agricultural and Resource Economics (ABARE), the effects on wheat, sheepmeat and dairy products are not expected to be significant in the short term. Luxury goods, such as abalone, rock lobster and prawns, will be particularly vulnerable to soft demand.¹⁶

Australia's export industry and its heavy reliance on a handful of commodities

6.14 Even though Australia's trade with Japan over the decades has diversified, it nonetheless is built around a tight cluster of core commodities. Throughout the 1990s, Australia remained heavily dependent on mineral and agricultural exports.¹⁷ Five commodities, all from primary industry, accounted for over half of Australian exports of \$16 billion in 1994—coal, beef, gold, iron ore and natural gas.¹⁸ In 1996, the export of non-monetary gold to Japan fell sharply and has not recovered. In 1997–98, Japan accounted for around 17% of agricultural, 17% of mineral and 42% of energy exports from Australia. The total value was in excess of \$8 billion dollars.¹⁹

15 Fuyuki Kitahara, Japan Chamber of Commerce, Sydney Inc, *Committee Hansard*, 3 September 1999, p. 802.

16 ABARE, submission no. 21, p.10 and comments by Dr Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 732; NSW Government, submission no. 25, pp. 10 and 14.

17 Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 731.

18 Richard Pomfret, 'Australian Experience with Exporting to Asia', *Seminar paper 96-01*, Centre for International Economic Studies, University of Adelaide, January 1996, p. 9.

19 Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 731. See also Barry Jones, Department of Industry, Science and Resource, *Committee Hansard*, 28 May 1999, p. 690.

6.15 The table opposite shows the value of the major commodities exported to Japan since 1994. The year 1996 shows a significant fall in the value of a handful of major items exported (*) to Japan and in large measure accounts for the 3% drop in Japan's share of Australia's export market.

Minerals and energy exports to Japan

Overview of Australia's mining and energy exports to Japan

6.16 The effects of the economic situation in Japan on exports of minerals and energy commodities to that country will continue to depend largely on whether the commodities are for final consumption in Japan or whether they are for processing and re-export.²⁰ For example, a substantial proportion of Australian exports of metals and metalliferous minerals, such as aluminium and base metals, is consumed in the building, construction, transport and public infrastructure industries. The Department of Primary Industries and Energy believed that these sectors were:

...most likely to be adversely affected by weak economic activity, the effects on Japanese consumption of these commodities in the current economic downturn could be quite significant.²¹

6.17 Despite the recent encouraging signs in the Japanese economy, weakness in domestic demands persists and public investment is still showing a downward trend. Given the subdued domestic demand in Japan, its final consumption of minerals and energy commodities is likely to remain flat until the economy recovers.²² Yet, even with this general softening of demand for Australian minerals and energy supplies, the effect is not spread evenly across all commodities.

Coal

Coal, Australia's major export earner, accounts for between 10% and 12% of total Australian exports, currently generating over \$9 billion per year in revenue. Japan is Australia's principal coal market. In 1992–93, Japan took half of all Australia's coal exports; in 1994–95 it took a 47% share; in 1995–96 a 43% share; in 1996–97 a 46% share before slipping further in 1997–98 to a 44% share. Coal exports to Japan went up marginally in value from just under \$4 billion to just over \$4 billion in 1998 and accounted for 42% of Australia's world wide coal exports.²³

20 Commonwealth Department of Primary Industries and Energy, submission no. 31, p. 7.

21 Barry Jones, Department of Industry, Science and Resource, *Committee Hansard*, 28 May 1999, pp. 691–2.

22 DKR, *Economic Report*, vol. 3, no. 2, 15 February 2000, p. 2; Barry Jones, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 691.

23 *Year Book*, no. 77—1995, p. 774; no. 78—1996, p. 680; no. 79—1997, p. 707; no. 80—1998, p. 775; no. 81—1999, p. 745; no. 82—2000, p. 791.

Table 6.2—Value of major Australian exports to Japan 1994–98

Export item to Japan	1994	1995	1996	1997	1998
	\$'000	\$'000	\$'000	\$'000	\$'000
Coal	3,180,896	3,165,031*	3,543,630	3,958,008	4,148,046
Confidential items ²⁴	1,285,947	2,309,104	2,663,733	3,040,989	2,955,058
Iron ore	1,218,685	1,296,587	1,311,026	1,583,244	1,788,544
Bovine meat	1,612,546	1,562,848*	1,113,188*	1,250,353	1,340,801
Aluminium	765,243	962,009	851,437*	1,143,116	1,257,596
Wood chips	448,463	562,812	530,795*	570,401	607,969
Non-monetary gold	1,372,252	1,197,934	466,299*	205,371	394,126
Copper ores	248,414	230,935	348,737	413,073	381,888
Crude petroleum	537,937	440,915	348,602*	333,802	336,139
Cotton	213,636	165,517	168,310	206,758	302,854
Machinery and transport equipment	305,162	272,590	286,902	317,648	294,714
Animal feed	225,601	229,757	269,209	304,817	293,506
Cheese and curd	148,423	169,853	204,308	215,544	276,263
Crustaceans	388,037	324,149*	309,518	313,876	244,961
Manufactures classified by material	203,516	216,302	210,602	208,360	244,255
Natural gas	1,023,205	759,132 ²⁵

24 The Australian Bureau of Statistics suppresses some detailed trade statistics for confidentiality reasons. The classification 'confidential items' in this table covers commodities such as sugar, rice, wheat and LNG.

Although the value of coal exports to Japan fell to \$A3.8b in 1999, Japan's share of Australia's export coal market increased to 45.1%.²⁶

6.18 While Japan is paramount to Australia as an export market for coal, Australia is important to Japan as a major supplier. Indeed, there is a strong interdependence between the two countries. Over the last decade, Australia has remained Japan's largest source of coal imports, supplying over half its coal needs. In 1998, it met 56% of Japan's coal requirements, a small rise from 52% in 1989.²⁷ In 1999, Australia's share of Japan's import market in coal rose to 57.1%.²⁸

6.19 Essentially, coal is used for steel production; for electricity generation; and for general industrial use—cement, paper manufacture etc.

Coking coal

6.20 The demand for coking or metallurgical coal, which goes into steel mills for steel production, has been falling in recent years. Forces independent of Japan's recession, however, are also at work influencing demand. Globally, coal for the steel industry is in over supply and demand is diminishing. Worldwide trends, especially in the area of technology and environmental concerns, are also influencing demand. Because of more efficient processes, the demand for coking coal is falling in Europe and also in Korea and Taiwan.²⁹ The pressure to lower costs is encouraging the steel mills in Japan and other countries to move to reduce their reliance on the higher quality and higher value coking coals.³⁰

6.21 Dr Christopher Rawlings, Managing Director of QCT Resources Ltd, explained the shift to other steel-making technologies that rely on less coking coal:

In the current downturn we are finding that many of the Japanese companies are taking alternative views to the selection of coking coal. They might take a lower quality coking coal or even a thermal coal to put into their coke blend. They are not that interested at the moment in productivity. Their major producing units—their blast furnaces and coke ovens—are really just ticking over. They are keeping them running; they are not running them

6.1

25 Market Information and Analysis Unit, Department of Foreign Affairs and Trade, *Composition of Trade Australia, 1998*, June 1999, p. 203. The value of wool exported to Japan has declined sharply from \$324,698 million in 1996, to \$310,032 million in 1997 to \$192,553 million in 1998.

26 Additional information supplied to the Committee by DFAT, 18 May 2000.

27 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/australia/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocument> (30 November 1999) (page 8 of 15).

28 Additional information supplied to the Committee by DFAT, 18 May 2000.

29 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 492.

30 See Denis Porter, NSW Minerals Council, *Committee Hansard*, 14 April 1999, p. 264.

hard. They have excess capacity in their steel industry—probably 30 per cent to 40 per cent above that actually produced at the moment. As such they have no need for the highest quality coals to drive those blast furnaces and coke ovens.³¹

6.22 It is against this background of over capacity not only in Japan but also in the world steel industry that negotiations have taken place on coking coal, which have produced reductions in both volume and price over recent years. In tonnes, Australia's coking coal exports to Japan went down by 5.1% on the 1997 level.³²

6.23 The prospects for coal and iron ore exports hinge on developments in the steel industry in Japan and also in the power industry. As major purchasers of these bulk commodities, Japanese steel makers exert a substantial influence on Australia's export performance. A recovery in steel production in Japan, will see a significant upturn in Australian exports of those products. Although much of the steel produced in Japan goes into export production directly or into products that are exported, signs for the Japanese steel industry are not promising. The most recent downturn in production translated into reductions in prices for iron ore and coal in the price negotiations that finished early in 1999. There were significant reductions in contract coal prices of up to 18% for hard coking coal, about 13% for steaming coal and iron ore prices of 10% to 11%.³³

6.24 At the beginning of 2000, some steel manufacturers were hopeful of a revival in their industry. Mr James Collins, policy adviser to the Steel Manufacturers Association, observed, however, that the basic problem of the world steel industry was an excess of steelmaking capacity which was 'hanging like an albatross over the world steel market.' Although steel makers in the United States, in particular, are optimistic for their own steel industry, the outlook for Japan is not so encouraging. Japanese producers have been scaling back raw-steel production to the lowest levels in decades in response to recessions in both their domestic market and in their other Asian export markets.³⁴

6.25 Indeed, in February 2000, BHP announced, in line with market expectations, that prices for the premium coal it sells to Japanese steelmakers would be reduced by

31 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 492.

32 Karen Gilmour, DFAT, *Committee Hansard*, 15 February 1999, p. 7; Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 265; Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/australia/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocument> (30 November 1999).

33 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, pp. 267–8.

34 James F. Collins, policy adviser of the Steel Manufacturers Association, 48th Annual Meeting of the American Institute for International Steel, 30 November 1999, in *New Steel*, January 2000, <http://www.newsteel.com/news/NW990114.html> (11 February 2000).

about 5% on average. This price reflects the current oversupply of coking coal for internationally traded premium hard coking coal, and it is expected that other major Australian coal suppliers would follow BHP in accepting a similar cut.³⁵

6.26 The drop in demand for coking coal has also dampened plans for new developments in Australia. QCT told the Committee that proposals for a \$470 million investment in new draglines and new coal washing technology had been pulled back and would probably not be more than about \$130 million or \$140 million.³⁶

Thermal coal

6.27 Japan is the world's largest importer of steaming or thermal coal, which is used in power generation. The coking coal market and the steaming coal market are moving in different directions at the moment. With continuing strong demand from Japan, which rose marginally in 1998 by about 1½% to 2%, Australian steaming coal exporters are more confident than their coking coal counterparts.³⁷

6.28 According to QCT Resources Ltd, thermal coal is increasing in demand worldwide at the rate of 6 to 10 million tonnes every six months. The predominant increase is in Asia. Although the demand curve has flattened slightly, there is still strong growth but, unfortunately, no increases in price. The falls in the contract price for steaming coal in 1998 was around 13%. Although disappointed, the NSW Minerals Council was not surprised given the depressed state of the Japanese steel industry.³⁸

6.29 Japan, which depends on more than 80% of its primary energy from imports, has a deliberate policy to diversify its range of power sources to achieve energy security. In relation to coal, the Japanese domestic coal industry is very small and at present, there are only two major underground coal mines in operation. Japan is dependent on overseas supplies for 97% of the coal it uses.³⁹

6.30 The two oil crises during the 1970s exposed the vulnerability of Japan's energy supplies which in turn strengthened its determination to spread its reliance on energy resources over a number of suppliers. Australian coal producers, who provide Japan with over half its coal requirements—about 60% of its steaming coal and about

35 Ben Ready, 'Coal prices forced down 5pc', *Canberra Times*, 8 February 2000, Business, p. 13.

36 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 492.

37 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, pp. 266–7.

38 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 492; Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 268.

39 United States Energy Information Administration, May 1999, <http://www.eia.doe.gov/emeu/cabs/japan.html> (16 February 2000); Katsuyoshi Ando, President JCOAL at 24th ICCR Meeting, Wellington, 18 and 19 October 1999, JCOAL Topics, no. 43, November 1999, http://www.jcoal.or.jp/e/Topics_E43.html (9 February 2000).

40% or 50% of its coking coals—sit uneasily with Japan’s policy to diversify its suppliers.⁴⁰ Nonetheless, Australia has established itself as a reliable and stable supplier and Australian coal producers are fully aware of the importance to maintain and enhance this reputation.

6.31 The projections that the Japanese Government has made in determining its energy needs for the future, particularly around the Kyoto debate, indicate that the only way they could fulfil their Kyoto expectations going on to 2010 was to build a large number of nuclear power stations. Nuclear energy provides the largest source of electricity in Japan, generating about 30% of their power. However, to increase nuclear generation substantially is going to be extremely difficult.⁴¹

6.32 Even though the Japanese Government is committed to nuclear power development, several accidents in recent years have aroused public concern and there is mounting unease in Japan about nuclear power generation.⁴² Furthermore, the lead times for construction are long and, according to QCT:

...they cannot even get site approval from the local population. Even if they tacked units onto an existing nuclear power station, they would not produce one-sixth of what is required under their proposed Kyoto proposal.⁴³

6.33 The Department of Industry, Science and Resources also expressed doubts about the Japanese Government’s predictions on future nuclear power generation. It told the Committee that the projections of the Ministry of International Trade and Industry (MITI) for Japan’s energy production are very different from the projections of some of the individual power companies. It surmised that if the MITI projections for the use of nuclear power are not realised, then there is the potential for an increase in coal prices and hopefully increased exports of LNG.⁴⁴ Moreover, if the Japanese

40 Mr Porter supplied the figures of 60% for steaming coal and between 40 and 50% for coking coals. Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 273.

41 MITI states that nuclear power accounts for 12% of Japan’s energy supply and 34% of electricity supply, MITI, ‘Energy in Japan’, (Overview), <http://www.miti.go.jp/introduction-e/a231201e.html> (16 February 2000). The United States Energy Information Administration, May 1999 states that ‘Of Japan’s total generation of electricity about 69% came from thermal (oil, gas and coal) plants, 20% from nuclear reactors, 10% from hydroelectric stations and 0.3% from geothermal, solar and wind’; United States Energy Information Administration, ‘Japan’, May 1999, <http://www.eia.doe.gov/emeu/cabs/japan.html> (16 February 2000). The Department of Primary Industries and Energy informed the Committee that Japan has undertaken to reduce its greenhouse emissions by 6 per cent from 1999 levels by 2008–12, Department of Primary Industries and Energy, submission no. 31, p. 23.

42 United States Energy Information Administration, May 1999; IEA, ‘Energy Policies of IEA Countries’, Japan, 1999, <http://www.iea.org/new/releases/1999/japan.htm> (16 February 2000); MITI, ‘Energy in Japan’, (Overview), <http://www.miti.go.jp/introduction-e/a231201e.html> (16 February 2000).

43 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 495. See also for example, ‘Cracks appear in nuke power policy’, *Mainichi Daily News*, 25 July 2000, <http://www.mainichi.companny.jp/english/news/news03.html> (26 July 2000).

44 Craig Burns, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 692.

economy emerges from its recession and there is a continuing growth in energy demand, the Japanese economy will look to electricity produced through coal and natural gas if the nuclear capacity is not there.

6.34 MITI expects coal consumption to grow by 1.2% per year, while utility companies estimate consumption will increase by 2.1% per year. Coal has, therefore, a very significant role to play as an energy source in Japan.⁴⁵ Australia is likely to be a beneficiary of this moderate growth, particularly as it has earned a strong reputation as a dependable supplier and is very aware of the need to improve the industry's environmental image.

6.35 At the centre of Japan's energy policy is the goal to attain the 3Es—energy security; economic growth; and environmental protection.⁴⁶ Australian commodity producers are clearly aware of, and sensitive to, Japanese concerns. QCT believed that cleaner coal from Australia burnt efficiently in modern power stations is far preferable than to have dirty coal coming from somewhere else burnt in open hearths. It told the Committee:

The challenge is that we do not seem to recognise in Australia that even with the Kyoto projections that we managed to negotiate, we have the capability of solving many other pollution problems by using clean Australian coal and new technology.⁴⁷

6.36 The Australian coal industry is serious about reducing greenhouse emissions and recognises that there is significant scope to lift efficiency, lower harmful emissions and at the same time improve coal's image as an environmentally acceptable fuel. Mr Robert Cameron, Chairman, Australian Coal Association, noted that the new generation of combustion technologies can dramatically reduce the SO_x, NO_x and particulate emissions and, through higher thermal efficiency, can reduce CO₂ emissions per unit of electricity generated. He acknowledged that the industry had accepted its responsibility to take 'commercially sensible actions' to minimise their greenhouse emissions and were acting to do so. He mentioned a number of agreements and research projects, such as the Greenhouse Challenge Program, intended to assist the industry in making coal a cleaner fuel.⁴⁸

45 United States Energy Information Administration, 'Japan', May 1999, <http://www.eia.doe.gov/emeu/cabs/japan.html> (16 February 2000); Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, pp. 494–5.

46 MITI, 'Energy in Japan', Overview, <http://www.miti.go.jp/introduction-e/a231201e.html> (16 February 2000)

47 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 495.

48 Robert Cameron, 'The Australian Coal Industry—Meeting the Challenges', Fifth APEC Coal Flow Seminar, Yokohama, Japan, 4 February 1999, pp. 9–10.

6.37 The Australian Government is also lending assistance to the Australian coal industry in its efforts to produce a cleaner coal. In June 1998, a joint three-year research program involving CSIRO and the Japanese Centre for Coal Utilisation (CCUJ) was established to develop an ‘ultra clean coal’ and to evaluate its commercial viability for Japanese customers. This project was an Australian initiative developed by White Industries and CSIRO’s Division of Energy Technology but will involve prominent Japanese companies, including Mitsubishi Heavy Industries, Idemitsu Kosan and Kyushu Electric Power Company. According to the Minister for Resources and Energy:

Coal is Australia’s most valuable export commodity, and this project is an excellent example of the benefits of fostering quality R&D Start program in the Industry, Science and Tourism portfolio.⁴⁹

6.38 The Committee fully endorses this type of government assistance particularly the joint nature of the project, which brings together both Australian and Japanese interests.

6.39 The debate in Japan about its fuel mix, including the country’s future demand for coal, will continue.⁵⁰ Even so, while there is a range of opportunities for power generation, including coal, nuclear power, natural gas and hydroelectric power, Japan looks on coal as one of its core energy sources among the alternatives to petroleum because of coal’s high level of supply security. Thus, coal has a vital and, for the moment, secure role in Japan’s energy mix.

6.40 Australia, with its rich coal reserves and efforts to make coal a cleaner fuel, is well placed to support Japan in pursuing its energy policy. Nonetheless, the current price for coal is depressed and there is continuing downward pressure on prices. Australia generally secures major long-term minerals and resources contracts with Japan. The market in thermal coal, however, is moving from a long-term contract market into a spot market. QCT explained that coal companies cannot switch on and off production units and they often have spare coal so, when they see a window in the market, they place that spare coal to get cash. A trend is now developing where ‘the pricing of thermal coal, in particular, is being sold at about, or in some cases just less than, the cash cost of production. So we are not seeing a full return—that is on an open and free market on a world basis.’⁵¹

49 See Senator Warwick Parer, Minister for Resources and Energy, Media Release, ‘Joint Australia-Japan Project to Develop Ultra Clean Coal’, 2 June 1998, DPIE 98/322P.

50 See for example Craig Burns, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 693.

51 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 6 April 1999, p. 493.

6.41 This shift is also occurring in the pricing system of steaming coal with customers tending to 'buy less on annual or multi-year contracts and more on a short-term basis—a spot or tender basis'.⁵²

6.42 While most observers understand Japan's preoccupation with securing its energy supply and its policy to diversify suppliers so as to enhance energy security, they can see drawbacks for producers such as Australia. Dr Mark Beeson noted that Japan's approach to diversification of supply means that it is:

...able to play off one producer against the other, so even if you are the cheapest supplier, as a matter of government policy they will encourage the principal buyers of coal in Japan not to put all their eggs in one basket and not to rely too heavily on one country. It is part of a government policy of economic security which they are particularly concerned about and they have very well developed strategies to ensure that they are never in a vulnerable position as far as producers are concerned.⁵³

6.43 It is important for Australia to be able to reassure Japan that it will remain a reliable supplier. Conversely, it is in Japan's interest to secure a steady and dependable supply. Japan requires energy imports and it is unlikely to discourage proven and reliable suppliers by putting up barriers. Nonetheless, Japan in its own interests will seek to improve ways to meet its energy requirements and will monitor other producers. So, there are possible challenges to Australian producers in terms of whether the Japanese, for example, might encourage natural gas production from the Russian Island of Sakhalin.⁵⁴

6.44 One positive aspect coming out of the present situation, however, is that while coal prices are low, coal is faring well in an extremely competitive energy market. Coal competes in countries such as Japan with other fuels, such as gas and nuclear power, and, because it is competitive, it has held or has even increased its share of the market.⁵⁵ Despite the current depressed market for commodities, Australian producers are looking to the long term. Put bluntly, QCT summed up the present approach taken by coal exporters in Australia:

When you look at the merchandising market and the commodities market in Australia, none of us feel too positive. We are really battenning down the hatches to hang in there. Everything we are doing at the moment is not

52 Denis Porter, New South Wales, Minerals Council, *Committee Hansard*, 14 April 1999, p. 264.

53 Dr Mark Beeson, *Committee Hansard*, 16 April 1999, p. 476. See Chapter 7, paras 7.70–7.77 for more information on how sale prices are negotiated between Japanese customers and Australian commodities producers.

54 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 275.

55 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 265.

about new investment; it is about trying to stay alive and keep the businesses running until we do see a turnaround.⁵⁶

Iron ore

6.45 Iron ore is one of Australia's major export commodities. It contributes about 4% to 5% of total Australian exports and in 1998–99 raised revenue of \$3.8 billion. Japan has a long-standing interest in importing Australian iron ore and has established itself as a most important market for this Australian commodity. In 1992–93, Japan took 49% of Australia's iron ore exports down from 54% in 1989. In 1995–96 this dropped to 45% and remained steady until it fell further to 44% for 1997–98 before recovering to reach 46% in 1998–99. In 1999, Japan's share of Australia's total iron ore exports stood at 46.7%, although the overall value of the iron ore had fallen. Despite these variations in the export share, Japan remains Australia's major market for iron ore followed by China and the Republic of Korea, which took 20% and 15% respectively of Australian total iron ore exports in 1998. The value of iron ore exported to Japan fell during the early half of the 1990s but, overall, has grown modestly from \$1.122 billion in 1989 to \$1.789 billion in 1998.⁵⁷

6.46 According to the Australian Bureau of Statistics, the fluctuations in the value of iron ore exports to Japan over the last decade were caused by changing contract prices, reflecting shifts in overall global supply and demand and increasing competition for market share, notably from Brazil. Nonetheless, Japan still looks predominantly to Australia for its supply of iron ore and, more recently, Australia's market share into Japan has begun to improve. In 1998, Australia provided 51% of Japan's iron ore imports, an increase from 44% in 1989.⁵⁸ In 1999, this share fell back marginally to 49.6%.⁵⁹

6.47 The falling demand in Japan for commodities, such as coal and iron ore, has placed downward pressure on prices. According to Hamersley Iron Ltd, Australian

56 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 505.

57 *Commonwealth Year Book*, no. 7—1995, p. 774; no. 78—1996, p. 680; no. 79—1997, p. 707; no. 80—1998, p. 775; no. 81—1999, p. 745; no. 82—2000, p. 791. See also Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.Australia/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocumen> (30 November 1999).

58 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.Australia/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocumen> (30 November 1999) (page 9 of 15). Hamersley told the Committee that Australia's market share in Japan has, over the last five years, recovered from roughly 48% to 53% to 54%, Philip Mitchell, General Manager, Strategic Marketing, Hamersley Iron Pty Ltd, *Committee Hansard*, 24 February 1999, p. 102.

59 Additional information supplied to the Committee by DFAT, 18 May 2000.

suppliers do not enjoy the dominant position they once did in coal and iron ore.⁶⁰ During lengthy negotiations with Japanese steelmakers in February 1999, Australian producers argued that a large price cut in iron ore would curtail new investment. Even so, Hamersley Iron had to settle for double-digit reductions in price for iron ore. This agreement effectively set the price for iron ore at 11% less than for the previous year.⁶¹ As with coal, this reduction in price was disappointing but anticipated given the weakened state of the Japanese steel industry.⁶² Nippon Steel explained the fall in 1999 prices:

...the harsh circumstances besieging the Japanese steel industry along with an expected decline in demand from other Asian nations have led to the settlement at a marked decrease in the price of both iron ore and coking coal.⁶³

6.48 Clearly, the depressed steel market is having an effect on Australian exporters but it is occurring through price rather than through volumes of exports.⁶⁴ Hamersley Iron Ltd explained that iron ore is basically priced pursuant to the rules applying to most commodities. The price is set at the point where the marginal producer is producing his marginal tonne.⁶⁵ Iron ore and LNG are sold on long-term contract to Japan. However, there is some flexibility in the volumes of those commodities which Japan takes—in the order of 10% to 15% within those contracts. Because the volumes are largely set within the contract, the adjustment to changes in demand tends to occur through price rather than volume. This arrangement accounts for all three major iron ore producers in Australia accepting cuts in their prices of between 11% and 13% in 1999.⁶⁶

6.49 Much of the steel produced in Japan is destined for export. Indeed, DFAT noted that the expected and anticipated price and volume cuts agreed to in on-going

60 Philip Mitchell, General Manager, Strategic Marketing, Hamersley Iron Pty Ltd, *Committee Hansard*, 24 February 1999, p. 91.

61 Prices were down 11% for fine ore, 10.2% for lump ore and 7.5% for lump premium, AME Mineral Economics, *Monthly Outlooks, Iron Ore*, February 1999.

62 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 268.

63 Nippon Steel, Business, Steel, <http://www.nsc.co.jp/english/business/steel.html> (15 February 2000). See also Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 160.

64 Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 160.

65 Philip Mitchell, General Manager, Strategic Marketing, Hamersley Iron Pty Ltd, *Committee Hansard*, 24 February 1999, p. 99 and Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 160.

66 See chapter 7, paras 7.70–7.75 for information on recent developments in the relationship between Australian iron ore producers and their Japanese customers.

negotiations reflects the global downturn particularly in steel as well as the Japanese recession.⁶⁷

6.50 According to QCT, the Japanese steel industry in 1998 achieved 102 million tonnes of crude steel production—hitting an historical low for the past 27 years—and predicted further falls in production. This drop in production translates almost directly into reductions in demand for iron ore. QCT had doubts about the Japanese estimates for production levels for the near future and feared further reductions would affect significantly the supply-demand balance and the price structure.⁶⁸

6.51 Because of a stagnant domestic economy and slow growth in regional markets, as well as tensions arising elsewhere because of excessive exports, Japan's outlook for 2000 is for the production of crude steel to remain flat with only a slight increase in production.⁶⁹ Up to this time, Australian commodities have held up quite well but the future, while not bright, shows some glimmer of hope. In February 2000, Robe River Iron Associates ratified a 4.35% increase for sinter fines with Japanese steel mills. This increase, described by a company spokesman as 'very satisfactory in the context of expectations late last year', suggested a 'strengthening in the steel market'. Moreover, it was a further recognition 'of Robe's consistent ability to deliver product on grade and on time'. Industry officials expected to see similar or slightly larger increases for lump ore.⁷⁰

6.52 Indeed, in March this year, BHP negotiated a price rise for both fines and lump ore. These new prices represent an average increase of over 5% and, though encouraging, still reflect 'Japan's difficult economic situation'. President of BHP Minerals, Mr Ron McNeilly, stated, 'The result, while positive, only allows us to recoup less than half the price cuts from last year, maintaining the pressure on iron ore producers to reduce costs and improve efficiencies to maximise returns on investment.'⁷¹

67 Karen Gilmour, DFAT, *Committee Hansard*, 15 February 1999, p. 7.

68 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, pp. 489–90. The US Geological Survey, *Mineral Commodities Summaries*, January 1999, provided the following statistics for raw steel production in Japan—1997: 105 million tonnes and in 1998: 95.1 million tonnes. DKR *Economic Report*, vol. 3, no. 2, 15 February 2000, p. 12.

69 *Metals News*, 15 July 1999, <http://www.manufacturing.net/magazine/purchasing/archives/1999/pur...071mnews.ht> (2 February 2000). See chapter 8 for a more detailed explanation about trade tensions arising from Japan's exports of steel.

70 North Ltd, Media Release, 29 February 2000, <http://www.north.com.au/news-releases/rel-2000022900.html> (7 March 2000); *Financial Review*, 4–5 March 2000, p. 12.

71 BHP, Press Release, 29 March 2000, http://www.bhp.com.au/press/bhp_press/data/20000329a.htm (30 March 2000). See also Ian Howarth, 'Strong Asian demand for iron ore steels Rio's quarter', *Australian Financial Review*, 29–30 April 2000, Business, p. 15.

6.53 The Australian iron ore sector must work within its own set of limitations and, as pointed out by Hamersley Iron, Australia has limited scope to stimulate demand for commodity exports. Nonetheless, it noted that Australia, despite the erosion of its position as a supplier, does have the capacity to influence supply. Even so, it observed:

In present circumstances, stimulating the supply of iron ore would only drive down the price of iron ore further. If you accept a philosophy that the Japanese buyers will always strategically constrain themselves to taking no more than 50 to 60 per cent of their iron ore supplies from Australia...then stimulating supply of further iron ore in this country will reduce Australian export revenues, because you push down the price but you do not actually push up the quantity.⁷²

6.54 Given that Australia's leverage is limited, Australia's national interest lies in doing whatever it can to prevent further deterioration in key markets. Maintaining Australia's reputation as a steadfast supplier is most important. Mr Timothy Marney, Director, Economic Policy, Treasury Department of Western Australia, underlined this point. He submitted that Australia's standing:

...has insulated us to some extent in that steel production has fallen in the order of 10 per cent yet our iron ore exports to Japan have continued to increase.⁷³

In other words, Australian producers have not suffered cuts in volumes of trade with Japan to the same extent as its competitors.

6.55 BHP noted the need to minimise costs and remove inefficiencies from the industry. Hamersley Iron agreed that this was a priority and pointed out that it was successfully reducing costs. It suggested that Australia continue to support the recovery efforts of Asian economies and maintain its pressure on Japan to accelerate domestic reform.⁷⁴

6.56 It was also put to the Committee that in a highly competitive global market, domestic costs should be kept to a minimum. It was suggested, for example, that rail reform and removal of barriers to competition in domestic markets would cut business costs and help create a dynamic business environment, which would encourage

72 Philip Mitchell, General Manager, Strategic Marketing, Hamersley Iron Pty Ltd, *Committee Hansard*, 24 February 1999, p. 92.

73 Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 160. See also Department of the Treasury, submission no. 63, p. 28.

74 Philip Mitchell, General Manager, Strategic Marketing, Hamersley Iron Pty Ltd, *Committee Hansard*, 24 February 1999, pp. 91 and 102.

Australians to embark on new ventures. Such measures would also benefit the whole community.⁷⁵

Aluminium

6.57 Aluminium is one of Australia's top five export earners and accounts for nearly 4% of Australia's total exports.⁷⁶ Japan is Australia's principal market for aluminium. In 1989, exports of aluminium to Japan were valued at \$1.4 billion which accounted for 11% of Australia's total exports to Japan and 55% of Australia's total exports of aluminium. By 1998, exports of aluminium to Japan had fallen 11% in value to \$1.251 billion. This represented 7% of Australia's total exports to Japan and 37% of Australia's total exports of aluminium. In 1999, the value of aluminium exports to Japan fell slightly and accounted for 33.4% of Australia's export market in aluminium.⁷⁷

6.58 Falls in the world aluminium price, a reduced Japanese demand and fierce competition from the United States, Brazil and the USSR were responsible for the substantial decline in the value of aluminium exports to Japan, especially during the early 1990s. Despite the overall decline in the value of exports, Australia remains one of Japan's major suppliers of aluminium. In volume terms, 24% of Japan's aluminium imports came from Australia in 1989, a slump followed with the share falling to between 15% and 17%, which rebounded in 1998 to 24% before falling back to 19.4% in 1999.⁷⁸

6.59 According to ABARE, the outlook for Japanese purchases of Australian aluminium in the medium term will depend on the extent of any return to growth in other markets, particularly in Asia. Total Japanese imports of aluminium are expected to rise relatively slowly.⁷⁹

Liquefied Natural Gas (LNG)

6.60 Since exports of LNG from the North West Shelf began in 1989, gas has gained in importance as an export earner for Australia. Between 1989 and 1994, exports of natural gas increased by 813%, from \$112 million to \$1.023 billion. By

75 For example, see comments by Mr Simon Wensley, Hamersley Iron Pty Ltd, *Committee Hansard*, 24 February 1999, p. 89.

76 Market Information and Analysis Unit, Department of Foreign Affairs and Trade, *Composition of Trade, 1998*, June 1999, pp. 13, 32.

77 Additional information supplied to the Committee by DFAT, 18 May 2000.

78 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocumen> (30 November 1999) (page 11 of 15). Additional information supplied to the Committee by DFAT, 18 May 2000.

79 ABARE, submission no. 21, p. 21.

1994, Japan was Australia's most important market for natural gas which accounted for 6% of total exports to Japan. Since August 1995, Australia's gas exports have come under confidentiality restrictions.⁸⁰

6.61 In 1999, Woodside, a participant in and operator of the North West Shelf Venture, announced that each year they sell 7.5 million tonnes of LNG worth more than \$1.5 billion in export income and that all but a few cargoes are sold under long-term contracts to customers in Japan. The North West Shelf Venture currently supplies, under long-term contracts, about 15% of Japan's LNG needs.⁸¹

6.62 Japan is a substantial joint venture partner in the operations in Western Australia in the North West Shelf. It is also heavily involved in developing infrastructure at the receiving end. The Treasury Department of Western Australia noted that the handling of LNG represents 'quite a significant investment' for the Japanese companies. It acknowledged this valuable and very significant contribution made by Japanese investment to LNG projects in Australia.⁸² Woodside informed the Committee:

We have eight Japanese buyers—five power companies and three gas companies. They are joined together in a consortium to give us long-term contracts, 20-year contracts for the sale of the LNG in order that we can invest the capital. The Japanese offtake was contracted at maximum and minimum rates and fortunately the Japanese customers took higher than their minimum rates right from the very start so that our build-up was faster than we had anticipated and we have had very strong support. That has continued even in these very difficult times and we are very conscious of the role the customers have played in our viability.⁸³

80 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/w.../bde7ace2081c70e6ca25677b00077c49?OpenDocumen> (30 November 1999) (page 8 of 15). The term confidentiality as explained in footnote 20 states that the Australian Bureau of Statistics suppresses some detailed trade statistics for confidentiality reasons and included commodities such as sugar, rice, wheat and LNG.

81 Woodside, 'Business and Finance News', 25 August 1999, <http://www.woodside.competition.Australia/business/News.cfm?ID=19990920115240> (18 February 2000). DFAT showed that, in 1999, Australia's share of Japan's LNG imports was 14.6%, additional information supplied to the Committee by DFAT, 18 May 2000. Erica Smyth, told the Committee that LNG generates about \$3 billion worth of annual export income. *Committee Hansard*, 25 February 1999, p. 205.

82 The six equal participants in the North West Shelf Venture are: Woodside Energy Ltd (operator); BHP Petroleum (North West Shelf) Pty Ltd; BP Developments Australia Pty Ltd; Chevron Asiatic Limited; Japan Australia LNG (MIMI) Pty Ltd; and Shell Development (Australia) Proprietary Limited. See also Erica Smyth, Woodside Energy Ltd, *Committee Hansard*, 25 February 1999, p. 211 and Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 161.

83 Erica Smyth, Woodside Energy Ltd, *Committee Hansard*, 25 February 1999, p. 207.

6.63 On a cost per unit, gas is not cheap because of the capital involved in producing LNG, its transportation and its receipt and storage at the other end. Nonetheless, Australian gas producers are able to help Japan achieve two of the most important goals underlying its energy policy—to secure a stable supply of energy and to protect the environment.

6.64 Australia stands on its record as a reliable supplier, a reputation supported by a very stable and predictable political climate.⁸⁴ In August 1999, the North West Shelf Venture celebrated its 1,000th cargo of LNG to Japan. Woodside announced this milestone as a ‘tribute to the excellent relationship which has developed over the past 10 years between the North West Shelf Joint Venture and the eight Japanese power and gas utilities which formed the foundation buyers’ consortium’. Reliability as a supplier was fundamental to this relationship with the Venture proudly proclaiming that in the 10 years of LNG exports, it had never missed a cargo.⁸⁵

6.65 Gas is also, according to Woodside, the greenest hydrocarbon and Australian gas can make a substantial contribution to the reduction of air pollution and ‘greenhouse emissions problems in the region’s major population centres by displacing coal and oil as energy sources’.⁸⁶ Thus, despite its relative high cost, LNG is a clean fuel and the LNG industry as a whole is very reliable. Clearly, Australia, as a major producer of LNG, has the potential to play a greater role in helping Japan meet its energy needs.

6.66 As noted earlier, if the MITI projections for the use of nuclear power are not realised, there is potential for an increase in coal prices and increased exports of LNG. The future of some of the significant LNG projects in Australia, particularly the North-West Shelf project, hinge on sales from increased LNG usage in Japan.⁸⁷

6.67 Stagnation of the Japanese economy is a major concern because Japan is the largest LNG buyer in South East Asia by a long measure. The dampened demand for commodities, such as LNG, influence investment and development. Woodside pointed out that the drop in demand for commodities had led to a review of investment in new developments for the time being. The contraction of the economy in Japan has slowed down Woodside’s anticipated schedule for expansion.⁸⁸

84 Erica Smyth, Woodside Energy Ltd, *Committee Hansard*, 25 February 1999, p. 205.

85 Woodside, ‘Business and Finance News’, 25 August 1999, <http://www.woodside.competition.au/business/News.cfm?ID=19990920115240> (18 February 2000).

86 Woodside, ‘Business and Finance News’, 25 August 1999, <http://www.woodside.competition.au/business/News.cfm?ID=19990920115240> (18 February 2000).

87 Barry Jones, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 692.

88 Erica Smyth, Woodside, Energy Ltd, *Committee Hansard*, 25 February 1999, p. 206.

6.68 Even so, the overall tightening of economic activity has provided incentive for the industry to increase its competitiveness by reducing operating costs. Woodside told the Committee that it is undertaking a major program of capital cost reductions and is working closely with Japanese buyers to try to streamline their project so that it melds with their needs.⁸⁹

6.69 In responding to suggestions about major infrastructure developments to assist Australia's export industry, QCT Resources was positive. It considered that the challenge was in finding finance for such large-scale schemes and that Australia should be doing something like that once every five years. It noted Australia's natural competitive advantages—cheap energy, good raw materials and a very good, innovative and productive Australian work force. In brief, QCT stated, 'we do not use them'.⁹⁰

6.70 The Committee is aware that industries in the mining sector have built up over the years a reputation as dependable and reliable suppliers—a standing that holds Australia in good stead with its Japanese customers, especially during this time of economic downturn. The Committee believes that the Australian Government and industry should continue to emphasise Australia's reputation as a competitive and reliable resource supplier in negotiations with Japan.

6.71 The Committee acknowledges the attempts of Australian industry and the Australian Government to work toward more environmentally sound means of producing their product or producing a product that will minimise harm to the environment. This is particularly so in research being conducted to produce cleaner coal. This is an area that requires research and education and one in which the Australian Government should take a lead.

Recommendation

The Committee recommends that the Australian Government encourage further joint research and development between Australia and Japan in the area of resource development and environmental protection.

Agricultural exports to Japan

Overview of Australia's agricultural exports to Japan

6.72 The complementarity that has been an enduring feature of the relationship between Australia and Japan in the mineral and energy sector also extends into

89 Erica Smyth, Woodside, Energy Ltd, *Committee Hansard*, 25 February 1999, pp. 206–7.

90 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, pp. 505–6.

agriculture. Japan is a resource poor but capital rich country while Australia, as a resource endowed country, is able to complement Japan's needs for raw materials and foodstuffs.

6.73 Japan's concern over its high dependency on imports to satisfy demand in minerals and energy extends to its policy on food supply. Japan depends on three countries—the United States, Canada and Australia—for more than 80% of major farm products, such as grains.⁹¹ The Japanese people hold food self-sufficiency as an indispensable part of their national security. According to the results of a recent public opinion poll, 80% of Japanese are concerned about the future food supply and 70% are willing to pay an additional reasonable cost for food so as to secure their food supply in the long run.⁹²

6.74 A report by the Japanese Investigative Council on Basic Problems Concerning Food, Agriculture, and Rural Areas highlighted Japan's heavy dependency on outside producers to feed its people:

Japan's food-self-sufficiency ratio has been on a continual decline. Japan's food self-sufficiency ratio was 42% in terms of calorie basis, or 29% in terms of grain in 1996, the lowest among major industrialized countries. The grain self-sufficiency ratio is the 135th highest among the world's 178 economies. In other words, Japan depends on farm imports for much of its food supply. In order to maintain its current diet, Japan depends on overseas farmland that is 2.4 times as large as the domestic one in a sense.⁹³

6.75 Governments, such as Japan's, which wish to protect their local products from imported goods choose from a range of trade barriers such as tariffs, quotas or a licensing system to keep imports at desired levels. Governments may also use various subsidies to domestic producers to give their home product a competitive edge. There is also a minefield of regulations governing matters such as quarantine and the distribution of products that may be used to limit or control foreign imports.

6.76 Food industries face a raft of regulations whenever they sell into the Japanese market. With beef, the Japanese apply a quota and tariff system which has been eased in recent years. Rice is subject to quotas and tariffs and sugar is confronted by a complicated system of licences, duties and levies. For many years, Australian wheat has enjoyed a secure market share of the Japanese market.

91 The Ministry of Agriculture, Forestry and Fisheries, Annual Report on Japanese Agriculture FY1998 (Summary) (Provisional translation).

92 Keiji Ohga, World Food Security and Agricultural Trade, paper presented in the OECD Workshop on Emerging Issues in Agriculture, Paris, October 1998.

93 The Report submitted to the Prime Minister by the Investigative Council on Basic Problems Concerning Food, Agriculture, and Rural Areas, September 1998, <http://www.maff.go.jp/ekihon/Report.html> (3 May 1999). See also Keiji Ohga, World Food Security and Agricultural Trade, paper presented in the OECD Workshop on Emerging Issues in Agriculture, Paris, October 1998.

Beef

6.77 Beef is one of Australia's major export commodities contributing to between 4% and 5% of Australia's total exports. Over the last decade, Japan has become a vital part of that export market. The value of Australian beef exported to Japan has almost doubled from \$773 million in 1989 to over \$1.3 billion in 1998 and almost \$1.4 billion in 1999. In 1989, Japan took 37% of Australia's beef exports; in 1992–93, 42%; which rose to 55% in 1994–95 before falling back to 47% in 1998 and 46.3% in 1999.⁹⁴

6.78 The significant rise in beef exported to Japan during the early 1990s can be attributed to a gradual liberalisation of beef imports since 1988–89, with the removal of quotas and the lowering of tariffs from 70% to 50%. Prior to that, Australian access was through essentially a quota system.⁹⁵ Factors, such as changing tastes and shifts in exchange rates, have also contributed to increases in demand for beef. According to the Australian Bureau of Statistics:

The sharp rise in beef exports to Japan up until 1994 reflected the combined effect of increasing consumer demand, gradual tariff reductions and the continued strength of the yen. The downturn in exports in 1995 and 1996 was due, in large measure, to an appreciating Australian dollar and growing competition from the United States of America. Between 1996 and 1998, the value of beef exports to Japan rose again due to slightly lower Japanese domestic production, a favourable exchange rate and higher US beef prices.⁹⁶

6.79 Despite the recent rise in the value of beef exported to Japan, the Japanese recession has dampened consumer demand and Japan's share of Australia's beef exports has remained flat though nonetheless substantial at around 47%.⁹⁷ The future for Australian beef exporters to Japan looks promising with the predicted downturn in

94 *Year Book Australia*, no. 77—1995, p.774, no. 78—1996, p. 680. Market Information and Analysis Unit, Department of Foreign Affairs and Trade, *Composition of Trade, 1998*, June 1999, p. 203. Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/with.../bde7ace2081c70e6ca25677b00077c49?OpenDocument> (30 November 1999) (page 10 of 15).

95 Dr Peter Barnard, Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, pp. 378 and 383.

96 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/with.../bde7ace2081c70e6ca25677b00077c49?OpenDocument> (30 November 1999) (page 10 of 15).

97 Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, pp. 378 and 381; and Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.au/with.../bde7ace2081c70e6ca25677b00077c49?OpenDocument> 30 November 1999 (page 10 of 15).

the United States' cattle cycle. The Meat and Livestock Association (MLA) suggested that Australia's market share will be either steady or increase further over the next four or five years.⁹⁸ In 1999, Australia held a substantial share of 37.8% of Japanese beef imports.⁹⁹

6.80 Notwithstanding the reduction in import quotas imposed by Japan on beef, solid impediments to trade remain. The MLA told the Committee that at the end of the Uruguay Round, beef tariffs into Japan will still be at 38.5% and the cost of that tariff to the Australian beef industry has been estimated at about \$200 million a year. It explained further:

Moreover, there are snap back provisions under which the tariff can revert back to 50 per cent if beef imports into Japan increase by more than 17 per cent. So those snap back provisions also create considerable uncertainty in the trade.¹⁰⁰

6.81 Accepting Japan's agreement to reduce the tariff to 38.5% by the year 2001, the MLA urged Australia to continue to promote agriculture as part of trade reform in regional trade agreements such as APEC, as well as in multilateral trade agreements. It stressed that the further reduction of tariffs must be of primary importance in the millennium round of the WTO. Put simply:

Australia needs to do all it can to pressure countries like Japan to reduce impediments to agricultural trade...we must do all in our power to pressure for reductions in tariffs and in trade impediments generally.¹⁰¹

6.82 In turning to the distribution system in Japan, the MLA noted that the system had undergone some rationalisation, but nonetheless regarded the system as 'probably still unduly complex'. The MLA's main concern, however, was with the tariff barriers rather than the non-tariff barriers.¹⁰² The question of access and import tariffs remains a priority for Australian beef exporters and is one that they will continue to pursue. According to the Australian Meat Council, it will join with all sectors of government and industry to try to achieve better access and lower tariffs.¹⁰³

6.83 Despite the obstacles confronting beef exporters, Australia has made considerable inroads into the beef market in Japan. The Australian beef industry is

98 Dr Peter Barnard, Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, p. 379. The Meat and Livestock Association is a new company and supersedes the Australian Meat and Livestock Corporation and the Meat Research Corporation.

99 Additional information supplied to the Committee by DFAT, 18 May 2000.

100 Dr Peter Barnard, Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, p. 380.

101 Dr Peter Barnard, Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, p. 385.

102 Dr Peter Barnard, Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, p. 384.

103 Stephen Martyn, Australian Meat Council, *Committee Hansard*, 15 April 1999, p. 381.

very aware and sensitive to the particular concerns of the Japanese consumer, particularly safety and quality matters, and has deliberately cultivated a good understanding with its customers. Again, the industry keeps in close touch with its customers' needs and changing tastes and works very closely with Japanese beef buyers. It invests much time, effort and money into consolidating the long-term relationships that are fundamental to maintaining market and commercial access into the Japanese market.

Rice

6.84 Although rice is not one of Australia's major exports to Japan, it nonetheless demonstrates some of the difficulties experienced by Australian exporters keen to improve access to the Japanese market. It also provides an interesting insight into Japan's strong concern about food self-sufficiency.

6.85 Rice has been the staple food of the Japanese for over 200 years. It is an integral part of Japanese culture and social structure and has a special significance for the Japanese people. As a rice-based culture, many Japanese feel strongly that Japan should be completely self-sufficient in this traditional staple food and even in the face of mounting international pressure, Japan has consistently baulked at opening its rice market to foreign competition.¹⁰⁴

6.86 Until 1995, Japan maintained an effective ban on rice imports. The agricultural ministry, through the Japan Food Agency, has the exclusive right to conduct trade in rice. Japan imported rice only when domestic production fell short of domestic demand as was the case in 1993 when unseasonable weather reduced the local rice crop. In reaching the Uruguay Round Agreement on Agriculture in 1995, however, Japan opted to import foreign rice under a minimum access quota system rather than adopt a tariffication of rice scheme. This agreement meant that Japan was required to import rice equal to a specified percentage of its annual domestic rice consumption. This percentage was to increase at an annual rate of 0.8% over the six year period from 4% in 1995 to 8% in 2000.¹⁰⁵

6.87 Although Japan is opening its markets to rice imports, the process of buying and selling rice in Japan is complicated and is closely regulated through the Japan Food Agency. The minimum market access quota is divided into two categories, ordinary quota and special quota or simultaneous buy and sell (SBS). The ordinary or

104 See Embassy of Japan to the United States, '“Rice Tariffication” Q&A' <http://www.embjapan.org/sf/rice.htm> (25 February 2000); David Askew, *Committee Hansard*, 17 May 1999, p. 544; Denis Gregory, 'Ricegrowers boil at Tariff', *Sun-Herald*, 2 May 1999, p. 71. See also Margaret Smee, submission no. 1, pp. 1–2.

105 Murata Yasuo, 'Working Around Rice Imports', *Japan Quarterly*, April-June 1999, p. 10; Shinichi Shogenji, 'Towards a Balanced Policy Framework for Food, Agriculture and Rural Areas: The case of Japan', http://www2.hasaii.education/apfat/PP09/iep_p09.htm (19 August 1999); Daily Summary of Japanese press, 14 December 1998.

regular minimum access is government business conducted by the Food Agency to add to the government's strategic stock holdings. The SBS is a more commercial transaction conducted by licensed trading houses through the Food Agency. Commencing with imports during the 1993 emergency period, the Ricegrowers Co-operative, Australia's dominant producer and exporter of rice, has successfully exported to Japan under both minimum access and SBS import mechanisms.

6.88 In the first SBS tender, in Japanese financial year 1995, Australia supplied 85,000 tonnes under minimum access and around 2,000 tonnes under SBS. By the end of the 1998 financial year, the Ricegrowers Co-operative had supplied to Japan around 350,000 tonnes of rice, worth on average around \$A240 million since 1995–96. In financial year 1998–99, Australia supplied Japan with 16% of its imported rice, over 14,000 tonnes through SBS and 87,000 under regular minimum assessment.¹⁰⁶ In 1999, Australia made up 18.1% of Japan's imported rice.

6.89 In December 1998, Japan announced that it would lower annual market access increases in the 1999–2000 periods from 0.8% of base consumption to 0.4% from 1 April 1999. These smaller increases set the import quota in 1999 at 644,000 tonnes instead of 682,000 tonnes, and in the year 2000 the quota will be 682,000 tonnes instead of 758,000 tonnes. Until another agreement is made, Japan's annual minimum access after the year 2000 will remain at 682,000 tonnes.¹⁰⁷

6.90 As part of this new import arrangement, the government now applies a tariff of ¥351.17 for each kilogram of imported rice that comes in above the minimum access level. This equates to around \$A4.47 per kilogram in 1999. This tariff will be reduced in April 2000 to ¥341 per kilogram, which is around \$A4.34 per kilo.¹⁰⁸

6.91 There is a clear suggestion that the imposition of such a high level of tariff is designed to thwart any further increases in rice imports into Japan. Many regard this fixed tariff of ¥351.17 per kilo on imported rice as prohibitive—intended to penalise foreign rice in the domestic market.¹⁰⁹ The Ricegrowers Co-operative argued:

Even a reduction in the year 2000 to ¥341 per kilo will not be enough to stimulate overquota trade. At a tariff level of ¥351 per kilo, Japanese buyers are unlikely to import any rice other than the premium outside the minimum access amount. With a very strong yen, the Australian dollar may be

106 In 1998–99, the US supplied Japan with 48% of its rice imports and Thailand with 21%, Australia had a 16% share and China a 11% share. *FAS Outline*, 'Foreign Countries' Policies and Programs', <http://www.fas.usda.gov/grain/circular/1999/99-02/dtricks.htm> (24 February 2000). See also Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 531.

107 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, pp. 531–2.

108 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 2.

109 Dr Aurelia George Mulgan, *Committee Hansard*, 28 May 1999, p. 680; Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, pp. 531–2.

competitive with top quality Japanese varieties. But regardless of the exchange rate, prices for standard quality Australian imports, including the ¥351 per kilo tariff, would not be competitive with domestic Japanese rice.¹¹⁰

6.92 Undoubtedly, the high tariffs are a formidable trade barrier. DFAT argued that the rice tariffication proposal would probably mean that while Australia could maintain its current level of rice exported to Japan, the tariff would cut down the potential for future growth.¹¹¹ Even so, the Ricegrowers Co-operative accepted that tariffication was a step in the right direction.¹¹²

6.93 At first, Australia objected strongly to the imposition of such a high tariff and, while welcoming Japan's intention to cease to apply special treatment for rice, expressed concern about the methodology used to calculate the rate of tariff which it argued was unfair.¹¹³ In March 1999, the Australian Government lodged a formal objection in the WTO. Yet one month later, it reversed its position, drawing criticism from the Federal Opposition for its inconsistency. The following explanation appeared in an article from *Asialine*:

...following a reappraisal of the technical aspects of the issue and in view of subsequent commercial developments, Australia decided to withdraw its objection and pursue its concerns on the level of tariffs in the WTO negotiations in agriculture, which are scheduled to commence at the end of 1999.¹¹⁴

6.94 Although rice consumption is declining in Japan, it will remain an important staple in the Japanese diet. The Japanese are becoming much more westernised but they are also becoming much more sensitive to health and the value of rice in the diet. Since the opening up of wheat and the introduction of wheat-based products, such as bread and noodles, to Japan, people have switched to those products because they are generally cheaper than rice. In light of the change in tastes and the price differentials between rice and alternative foods, the current pricing arrangements and quota systems do not encourage increased consumption.

110 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 532.

111 Colin Heseltine, DFAT, *Committee Hansard*, 15 February 1999, p. 12.

112 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 532.

113 The Hon Tim Fischer, MP, Deputy Prime Minister and Minister for Trade, Media Release, 'WTO Rice Tarrification Response', 19 March 1999 and WTO Summary Report of the Meeting held 12–26 March 1999, G/AG/R/18. The level of tariff has been calculated by comparing the value of imports in the Uruguay Round base period, 1986–88, with the value of the local product over the same period. At the time of the base period being set, Japan was only importing lower quality broken rice, particularly from Thailand, for industrial use.

114 Country Information, Japan, 'Australia's Rice Exports Continue to Perform Strongly', Article from *Asialine*, June 1999, http://www.dfat.gov.au/geo/na/japan/articles_asialine_rice.html (28 February 2000).

6.95 The population of farmers in Japan is ageing quite rapidly and the average size of a farm in Japan is very small at little more than one hectare. The new agricultural basic law will not allow large companies such as Mitsubishi and Mitsui to buy up huge tracts of Japanese land and conduct company farming. Rather, it is intended to allow groups of farmers who are currently producing agricultural commodities to turn themselves into companies. 'It is a kind of a collective agriculture, but it is private'. The rice growing industry in Japan will ultimately need to undergo radical change.¹¹⁵

6.96 Even though exporting rice to Japan can be frustrating at times due to the complicated import mechanisms which remain heavily controlled by the Ministry of Agriculture, Forestry and Fishery through its Food Agency division, the Ricegrowers Co-operative remains committed to the Japanese market. It accepts that, in Japan, rice is an extremely sensitive issue of great political importance. Furthermore, it acknowledges the efforts that the Japanese Government is making to liberalise this highly sensitive industry and it looks forward to future growth. It sees a need for government involvement in facilitating trade and a partnership between the Australian industry and the Australian Government. For example, there is still much to be done towards the liberalisation of trade in agriculture through the next round of the WTO. The Ricegrowers Co-operative told the Committee:

If we are not successful in having further agreement from Japan on liberalising its market through that round, then it will be many years down the track before we will have another opportunity.¹¹⁶

Sugar

6.97 Raw sugar is Australia's second largest crop export after wheat with annual export sales in 1997–98 of \$1.7 billion. This accounts for 85% of the industry's production. With gross value of sales exceeding \$2 billion annually, sugar is Australia's fifth largest rural industry, based on gross value of production, after wheat, beef, wool and dairy.¹¹⁷

6.98 Throughout the 1960s, sugar was one of Australia's top export commodities to Japan but in the 1970s it started to lose ground and during the 1980s its value as an export declined markedly. In contrast, products such as meat and fish were gaining a larger share of Australia's export market to Japan. Although sugar is no longer a major export to Japan, Australian sugar exporters would like to improve their access to this market and, furthermore, ensure that the demand for sugar in Japan does not

115 Aurelia George Mulgan *Committee Hansard*, 28 May 1999, p. 684; Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 539; Dr Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 664.

116 Bernard Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 540.

117 Warren Males, Queensland Sugar Corporation, *Committee Hansard*, 16 April 1999, p. 454.

suffer because of regulations. In 1999, Australia's share of Japan's sugar imports was an impressive 39.6%.¹¹⁸

6.99 Difficult hurdles confront those wishing to import sugar into Japan. As with rice, the Japanese Government is seeking to shield local producers from foreign competitors. The Queensland Sugar Corporation (QSC) told the Committee that it is keen to continue its strong marketing ties with Japanese customers. It is, however, concerned about the effects of the sugar price stabilisation law on Japan's domestic sugar market—in particular, on consumption and import levels. Mr Warren Males Principal Economist, QSC, explained this legislation:

Under the law, import prices are increased to domestic price levels through the activities of the Agriculture and Livestock Industries Corporation which is known through its acronym of ALIC. Each importer is required to sell all imported sugar to the ALIC at the average import price current at the time of the import declaration. In a simultaneous transaction the ALIC sells back the same sugar to the same importer at a higher price, which includes import duties, levies and surcharges. The levies and surcharges collected are used to produce the subsidies to encourage production.¹¹⁹

6.100 According to QSC, the law is not achieving its stated objectives. Under this law, domestic prices are maintained at levels significantly higher than the world price—almost 20 times the world level. These high domestic prices are altering the structure of sweetener consumption in Japan where alternative sweeteners are being substituted for sugar.

6.101 In the face of falling world sugar prices and the lower tariff levels, Japan has increased the surcharges imposed on imported sugar leaving the high domestic prices largely unchanged. With domestic prices stabilised, sugar users in Japan have not received any price incentives to increase their sugar consumption.

6.102 The irony, as pointed out by QSC, is that even though total sweetener consumption is steady in Japan at around 3.3 million tonnes a year, these high domestic sugar prices have reduced sugar's share of the sweetener consumption in Japan and caused a switch to alternative sweeteners and to sugar blends. It argued that, while sugar prices have been stabilised, this has been at an enormous cost to the Japanese consumers and the world sugar trade. The law has succeeded in discouraging consumption and increasing competition from substitutes. Put bluntly it asserted:

The higher prices are not sufficient to increase domestic sugar production. Self sufficiency has not been achieved. Sugar imports have fallen.¹²⁰

118 Additional information supplied to the Committee by DFAT, 18 May 2000.

119 Warren Males, Queensland Sugar Corporation, *Committee Hansard*, 16 April 1999, p. 454.

120 Warren Males, Queensland Sugar Corporation, *Committee Hansard*, 16 April 1999, p. 456.

6.103 Consequently, there has been strong growth in imports of sugar-containing products and imports of maize and other starch-based products which do not attract such high duties or levies. QSC argued that the Japanese Government is reluctant to reform its sugar policy beyond the bare minimum requirements under the WTO. The Queensland raw sugar industry is seeking liberalisation of the current sugar regime in Japan. It insisted that ‘Australia must lead the charge on trade reform in sugar’.¹²¹ It suggested that an ad valorem tariff would be preferable to the complicated system of duty, surcharges and levies contained in the stabilisation law. A tariff would allow domestic prices to reflect changes in world prices albeit at a higher level.

6.104 The QSC stressed the point that Australians need to encourage an open and honest discussion of the merits of current sugar policy regimes, their effectiveness and implications for world trade. It stated further:

...we are not disputing the Japanese government’s ability to support its domestic industry. We would like to see them provide that support in a way which is transparent, in a way which enables the producers to respond to price decisions in their production decisions.¹²²

6.105 One approach suggested by Mr Philippe Ingram, Manager, Japan Secretariat, Department of State Development, Queensland, would be to open up public debate in Japan about protectionism. Drawing on his experience, he told the Committee that most Japanese are not aware of the importance of trading issues, such as the beef and rice tariff, to Australians because ‘95 per cent of them live in big cities and they do not know where their food comes from anyway’. He submitted that there ‘are ways of explaining to the public how they benefit from liberalisation, which I do not think the Japanese government has done at all’.¹²³

Wheat

6.106 Australia is a small producer of wheat but a large trader and exporter. In 1995–96, wheat accounted for 4% of total Australian exports; in 1996–97 it jumped to 5% before settling back to 4% of total exports in 1997–98 and in 1998–99 it raised revenue of \$3.4 billion.¹²⁴

6.107 Japan is a major purchaser of Australian wheat and since the 1960s, it has consistently taken about a million tonnes of wheat every year. Wheat is regarded in Japan as an important staple and is classified as an item of state trading. As such, its

121 Warren Males, Queensland Sugar Corporation, *Committee Hansard*, 16 April 1999, p. 454.

122 Warren Males, Queensland Sugar Corporation, *Committee Hansard*, 16 April 1999, p. 467.

123 Philippe Ingram, Department of State Development, Queensland, *Committee Hansard*, 16 April 1999, p. 412.

124 *Year Book* no. 79—1997, p. 707; no. 80—1998, p. 775; no. 81—1999, p. 745 and no. 82—2000, p.791. Note principal market information is confidential—see footnotes 20 and 78.

importation comes under the strict control of the Japan Food Agency (JFA). Despite the downturn in the Japanese economy, wheat exports are not expected to be greatly affected in the short term.¹²⁵

6.108 Under the Wheat Marketing Act 1989, the Australian Wheat Board Ltd (AWB) has been delegated single desk export authority which means that it is the sole exporter of wheat from Australia. The AWB enjoys a special arrangement with the Japanese Government, through the JFA, which allows Australian wheat exporters access to the Japanese market. The JFA values its dealings with Australian wheat growers because they provide security of supply and a high quality product and service. In return, Australian producers are rewarded with a 'virtually guaranteed access' to this prized market. Australia's market share in Japan has been stable at between 19% and 20% and is fortunate to be amongst three overseas countries sharing this market.¹²⁶ As explained by Mr Simon Burgess:

...there is no doubt the arrangement that is currently in place effectively apportions a share of the trade to America, Canada and Australia.¹²⁷

6.109 Hence, unlike beef, rice and sugar exporters who experience difficulties in getting their products into Japan, wheat growers are not directly concerned about impediments to trade regarding importing wheat into Japan.¹²⁸

6.110 The AWB has been aware of Japan's concern over food security.¹²⁹ It explained:

...in terms of their heavy reliance on exports, they continue to have to feed their population, so we are probably a little bit buffered from both the internal and external economic turmoil in the region. That, I suppose, has given us a much steadier keel...I would not expect a major change in the long term.¹³⁰

6.111 The AWB has also been fully cognisant of the pressure on the Japanese to deregulate their market and it acknowledged that some Australian exporters, such as rice and sugar growers, have a strong interest in further deregulation. For wheat growers, however, there is a choice between the stable market share they now enjoy or

125 Simon Burgess, Australian Wheat Board, *Committee Hansard*, 19 February 1999, pp. 76, 83; Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 732; Australian Wheat Board Ltd, submission no. 27, p. 6.

126 Simon Burgess and Andrew McConville, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, pp. 75–6, 81; Grains Council of Australia, submission no. 24, p. 1.

127 Simon Burgess, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, pp. 80–1.

128 Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 732.

129 Simon Burgess, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, p. 85.

130 Andrew McConville, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, pp. 86–87.

a possible larger share of the cake. The AWB and the Australian Grains Council believed that Australia should not push for the dismantling of the JFA because of Australia's long established and close relationship with this organisation. Overall, the AWB considered that deregulation would not benefit Australian wheat growers and that the dismantling of the JFA could result not only in stiffer competition in the Japanese market but also the possibility of losing the premiums Australian wheat growers enjoy. Mr Burgess conceded that there is a trade-off 'as to what our share is and whether we buck the system to push for deregulation'. The AWB recognised, however, that Australian wheat producers do need to be prepared for deregulation to ensure that they are well positioned to take advantage of any such reform.¹³¹

6.112 AWB's priorities in terms of the next round of the WTO are focused not on the Japanese barriers to trade but on the actions of major competitors, the US and the European Union in particular, in providing high levels of domestic support arrangements and export subsidies to their local producers.¹³² This places producers such as Australian farmers, who do not benefit from government subsidies, at a disadvantage in the international market.

6.113 In common with many other producers, Australian wheat exporters understand that the Japanese are willing to pay a premium for quality. Thus, they have decided to concentrate on producing wheat that gives them a comparative advantage over their competitors—wheat for noodle production. Although Australia supplies some of the highest quality wheat to Japan, the AWB nonetheless is looking at developing new and different wheat and at ways of improving the products that they produce with Australian wheat. It works with the JFA to develop specific products.¹³³

Wool

6.114 The Australian wool industry dominates the world market for wool. Australia produces one-third of the world's total wool production, half the world's wool that goes into clothing and 70% of the world's merino wool. Wool is a significant export earner for Australia.¹³⁴

6.115 The industry is exposed to global economic circumstances. The 1990s was a difficult decade for wool with a collapse in demand in key consuming countries in Eastern Europe and economic stagnation in Western Europe and Japan. More recently, the Asian crisis and the downturn in China has further eroded demand for wool.

131 Simon Burgess, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, pp. 77–8, 80–81.

132 Andrew McConville, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, p. 82 and the Grains Council of Australia, submission no. 24, p. 2.

133 Andrew McConville, Australian Wheat Board Ltd, *Committee Hansard*, 19 February 1999, pp. 83–4.

134 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 507.

6.116 Australian wool exports to Japan have fallen markedly in value over the last decade. Japan is a vital market for Australia's wool and the decline in its economy in the 1990s seriously affected Australia's wool industry and contributed substantially to its problems.¹³⁵ Ten years ago, Japan was the number one export destination for Australian wool. In 1989, Australia exported wool valued at \$1.004 billion to Japan. This represented 8% of Australia's total exports to Japan and 20% of Australia's world-wide wool export market. By 1998, the value of Australian wool exported to Japan stood at just \$193 million, a fall of 81% over the ten year period. This accounted for only 1% of Australia's total exports to Japan and 7% of world wide wool exports. In 1998, China was the primary destination for Australian wool, accounting for over 20% of exported wool. Italy was Australia's second most important wool buyer taking over 18% of Australian wool.¹³⁶ In 1999, the value of wool exports to Japan fell further to \$154 million. Despite the sharp decline in the value of wool exported to Japan, Australia is still Japan's principal supplier of wool accounting for 34.8% of Japan's total wool imports for 1999.¹³⁷

6.117 The fall in the value of wool exports to Japan is due to a combination of factors—a decline in final consumption of wool because of Japan's economic problems; high stocks of semi-processed wool, loss of competitiveness in Japan's wool processing industry and a shift in location of processing away from Japan to other more cost-effective countries; including China, Korea, Taiwan, Thailand, Malaysia and Australia.¹³⁸

6.118 Japan's wool processing industry is finding it difficult to compete with these countries, particularly given that its labour costs are amongst the highest in the world in the textile industry—five or six times as much as in other countries such as China,

135 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 508.

136 Market Information and Analysis Unit, Department of Foreign Affairs & Trade, *Composition of Trade Australia, 1998*, Canberra, p. 30. The value of Australian wool exported in 1998 was \$2.872 billion with China taking \$591 million and Italy \$539 million.

137 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.Australia/with.../bde7ace2081c70e6ca25677b00077c49?OpenDocumen> (30 November 1999) (page 10 of 15). The ABS gave the unusually high figure of 79% for Australia's share of Japan's wool imports in volume terms for 1997–98. According to Woolmark, a decade ago wool had about a 17% share of Australia's exports. By 1997–98 it had fallen to fifth place with a 6% share. Australian exports to Japan totalled about \$259 million in 1997–98 compared with 1.29 billion 10 years ago. Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 508. DFAT stated that Australia's wool share fell in 1998, but it was still almost 48% of the Japanese market. See Karen Gilmour, DFAT *Committee Hansard*, 15 February 1999, p. 21.

138 Australian Bureau of Statistics, 'Australia Now—A Statistical Profile', International Accounts and Trade, Feature Article—Australia's merchandise trade with Japan, <http://www.statistics.gov.Australia/with.../bde7ace2081c70e6ca25677b00077c49?OpenDocumen> (30 November 1999) (page 10 of 15) and Mr Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 508.

Thailand and Malaysia.¹³⁹ Fully aware of their uncompetitive production costs, especially in the early stage processing, Japanese wool processors have invested substantially in these more cost-effective countries.

6.119 Thus, Japan is increasingly importing products in either final form or as fabric and yarn. Imports of products, such as yarn, fabrics and garments, have increased from 41% in the early 1990s to 64% in 1998.¹⁴⁰ Despite this trend, according to the Woolmark Company, Japan will remain a significant manufacturer of high-quality yarns and fabrics and will import the 'run-of-the-mill' yarns, fabrics and clothing.

6.120 The substitution of cotton and synthetic fibres is another factor undercutting demand for wool and forcing down world export prices. In essence, the key to wool sales is final demand—the garments that end up in wardrobes—and Japan's final wool consumption has declined by 25% through the 1990s. This huge drop in such an important market is due mainly to the very difficult economic situation in Japan.¹⁴¹

6.121 During a period of economic downturn, price competitiveness also comes into play and consumers will become even more price conscious where value for money becomes a major consideration. The wool textile pipeline tends to be more costly than the equivalent for cotton and synthetics, with wool garments asking about twice the price of the equivalent in other fibres. Thus wool garments are particularly income sensitive which means that the poorer the income growth rates the lower the wool consumption as consumers turn to more price competitive products, including synthetic fibres. This pattern is particularly evident in Japan, where synthetic fibres have usurped a significant share of the Japanese final market from both wool and cotton. Producers of synthetic fabrics have won over consumers with their innovation in devising new attractive products that have flair and style.¹⁴²

6.122 Changing fashions and tastes, such as the trend away from formal wear to more casual styles, are affecting the demand for wool garments. Demographic trends are important also, particularly in Japan with its ageing population as well as the move away from buying clothing in favour of electronics, travel and so on.

6.123 The challenge for wool is to adapt to the changes occurring in the Japanese lifestyle and in the fashion market—to create interest in, and demand for, wool garments. The Woolmark Company is prepared to meet this challenge and is looking to develop and promote innovative wool products in Japan to appeal to the smart casual and active leisure wear market and generally to respond to consumer trends, for

139 Dr Terence Sheales, ABARE, *Committee Hansard*, 21 June 1999, p. 732.

140 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 508.

141 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 508.

142 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, pp. 508–9.

example, in wool blends that retain the reputation for quality but are less expensive.¹⁴³ The Woolmark Company submitted that, because of Japan's lead role throughout Asia in wool processing, it has established a development centre in Ichinomiya to speed up the adoption of new products in Japan and throughout the rest of Asia.¹⁴⁴

6.124 Japan is a well-established trading partner particularly through the large trading houses. The closure of one of the large Japanese trading houses, Nissho Iwai, in May 1999 reflected the much lower volumes of trade, particularly in raw wool production.¹⁴⁵ There is an over capacity in many sectors of the wool textile pipeline, particularly in early stage processing where there is about a 25% or 30% over capacity worldwide. This situation is encouraging a fundamental restructuring of the industry.¹⁴⁶ Even so, a revival in economic growth would boost demand for wool.

6.125 There has been a shift in Australia in the early stage processing—scouring and production of tops. About a third of Australia's raw wool is now turned into some value added product in Australia and then exported. According to the Woolmark Company, there is some interest in yarn production but the key challenge for the Australian textile industry is the high labour costs and the fact that we already have established customers around the world, such as Italy, who want to buy a raw product.¹⁴⁷

Trade liberalisation and agriculture in Japan

6.126 Clearly, a boost in Japan's economy will give encouragement to many Australian exporters. But for the agricultural sector, as noted by the beef, rice and sugar industries, trade liberalisation is most important. The powerful agricultural lobby groups in Japan make it particularly difficult to move this process of deregulation ahead. The development in Japan of approaches to so-called non-trade issues, including social and environmental matters, which are most commonly placed under the heading 'Multifunctionality of agriculture' is an area of great significance for future multilateral negotiations. It is an area fraught with risk for Australia's efforts to achieve greater liberalisation of agricultural trade in the WTO.¹⁴⁸

6.127 The Japanese Government believes that appropriate levels of agricultural production should be maintained in Japan to enhance the environmental benefits of agriculture including the prevention of soil erosion, landslides and floods and for the

143 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 509.

144 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 512.

145 Cathy Bolt, 'Japan wool buyer bales out from Australia', *Financial Review*, 4 May 1999.

146 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 511.

147 Christopher Wilcox, The Woolmark Company, *Committee Hansard*, 17 May 1999, p. 517.

148 Dr Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, pp. 659–60.

conservation of its water resources. In defending its stand on the ‘multifunctionality of agriculture’, the Japanese Government argues strongly that agriculture in Japan warrants government support, including border measures, to ensure that its functions go beyond merely producing food to embrace other aspects that benefit society such as maintenance of the ecosystem, conservation and rural development.¹⁴⁹

6.128 At a time when Australia is looking to expand its agricultural market through trade liberalisation, Japan is sending mixed messages. In May 1999 the Japanese Ministry of Agriculture, Forestry and Fisheries (MAFF) explained that it wanted to see ‘truly fair’ trade rules established. It wanted, however, the principle of ‘multifunctionality of agriculture’ to inform any such rules set down in the WTO negotiation on agriculture.¹⁵⁰

6.129 While food security, environmental protection and the wellbeing of agrarian communities are legitimate concerns for the Japanese people, such arguments could also be used to justify the sorts of very high levels of protection that still exist in Japan. The OECD has developed a producer subsidy equivalent (PSE) which measures the percentage of a farmer’s income made up of government assistance. Japan’s average PSE is high at 69% compared to Australia’s which is 9%. The OECD average is 34%. Even for a highly protected region like the European Union, the figure for average PSE is 42%.¹⁵¹

6.130 The Japanese agricultural lobby seeks aggressively to maintain a highly protected Japanese agricultural sector. While the influence of that lobby group may have waned, there is the prospect that the WTO agricultural negotiations will spur it to renewed efforts to shield Japan’s agricultural sector from outside competition.

6.131 Japan’s overall lack of a firm commitment to trade liberalisation in agriculture has become increasingly apparent since the APEC leaders meeting in Kuala Lumpur in 1998 when Japan managed to give only equivocal support for the early sectoral liberalisation initiative and agreed to refer the matter to the WTO. Indeed, toward the end of 1999 as the WTO negotiations approached, food security loomed large as a major preoccupation for Japan and was raised during the WTO ministerial conference in Seattle. During this session, Japan told Ministers at the meeting that the WTO must address issues arising from the impact of trade liberalisation on matters such as ‘environmental protection, food safety, the maintenance of agrarian communities, and the preservation of culture and tradition’. It stressed the importance of giving due consideration to redressing ‘the imbalance of rights and obligations between food

149 For a definition of ‘multifunctionality of agriculture’ see, MAFF Update, No. 309, 14 May 1999, <http://www.maff.go.jp/mud/309.html> (17 March 2000).

150 MAFF Update, No. 309, 14 May 1999, <http://www.maff.go.jp/mud/309.html> (17 March 2000).

151 Dr Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 661.

importing and exporting countries' as well as the multifunctionality of agriculture.¹⁵² The disappointing outcome of the WTO talks in Seattle at the end of 1999, when talks were suspended, makes the concerted effort by both Japan and its trading partners to resume the WTO agriculture negotiations all the more important for Australia.

6.132 Given that Japan is Australia's most important export market for agricultural products, it is important that Japan remains committed to agricultural trade liberalisation, the dismantling of non-tariff barriers and rejection of protectionist policies. Japan's recent decision to set the rice tariff at 390% for rice imports is not a promising sign for future trade liberalisation nor is the emphasis it chose to give to food security and the multifunctionality of agriculture during the WTO talks in Seattle.

6.133 The Committee believes that to safeguard and promote its trading future, Australia must continue to argue in international fora for the liberalisation of trade, particularly in agriculture. It found the decision by APEC to refer the early sectoral liberalisation initiative to the WTO as a second best option and, in light of the lack of progress at the Seattle meeting of the WTO, believes that APEC should once again pursue this matter with determination.

Recommendation

The Committee recommends that the Australian Government, with renewed effort, seek the cooperation of countries such as Japan to reinvigorate the APEC process in setting down achievable goals toward the realisation of trade and investment liberalisation.

6.134 The Committee acknowledges the need to continue to encourage Japan to liberalise its highly protected agricultural markets, which includes going beyond its Uruguay Round commitments on trade liberalisation and to implement greater reforms on market access and domestic support. It found the failure of the third WTO ministerial conference to launch a new round of multilateral trade negotiations regrettable and the lack of leadership shown by the world's leading economies disappointing.

152 Statement by H.E. Mr Yohei Kono, Minister for Foreign Affairs, Ministerial Conference, 1 December 1999, WTO WT/MIN(99)/ST/26.

Recommendation

The Committee recommends that the Australian Government urge like-minded countries seeking greater liberalisation in agricultural trade to lobby for the commencement of the new round of WTO trade talks at the earliest possible date.

Export of services to Japan

Overview of Australia's trade in services

6.135 Service exports grew steadily throughout the 1990s and, although Australia remained a net importer of services, the size of the net import ratio has declined. This shift from being a 'persistent net importer to a net exporter' is due in large measure to Australia's growing tourism industry and to a lesser extent the export of education services. In 1996, one economist predicted that the demand for both these services 'could exhibit bandwagon effects as more satisfied tourists and students report home and as Australian suppliers become more attuned to Asian customers.'¹⁵³

Export of services to Japan

6.136 Since 1987–88 and up till very recently, Japan has been the principal destination for Australian services exports. The growth rate in the export of services to Japan has slowed since 1991–92, due in the main to the downturn in the Japanese economy.¹⁵⁴

6.137 In 1995–96, the value of exports of services to Japan reached \$3.9 billion accounting for 17% of total Australian services exports. Although the value of Australia's exports in services to Japan fell to \$3.7 billion in 1996–97, it nonetheless represented 15% of Australia's total export of services and was higher than the value of service exports to the United States, which stood at \$3.2 billion or 13% of Australia's total services exports. In 1997–98, however, the United States pipped Japan as Australia's main destination for services exports with the value of Australia's exports of services to Japan at under \$3.6 billion while the United States had jumped ahead with a value of \$3.9 billion.¹⁵⁵ This gap further widened in 1999 with the value of exports of services to Japan falling to \$3.4 billion or 12.3% of total services exports

153 Richard Pomfret, 'Australian Experience with Exporting to Asia', *Seminar paper 96-01*, Centre for International Economic Studies, University of Adelaide, January 1996, pp. 11–13.

154 Department of Foreign Affairs and Trade, *Trade in Services, 1995-96*, p. 5.

155 Market Information and Analysis Unit, Department of Foreign Affairs and Trade, *Trade in Services 1996-1997*, p. 6; *Trade in Services, 1997-98*, pp. 9, 13.

and the value of exports of services to the United States rising to \$4.6 billion or 17% of Australia's total exports of services.¹⁵⁶

Tourism

6.138 In-bound tourism, has been a core component of Australia's export services for many years and has increased strongly since the mid 1980s.

6.139 The rise of Japan as an important tourist source market for Australia started in the mid-1980s. In 1986, 145,000 Japanese visited Australia and this rose to 215,000 in 1987.¹⁵⁷ Indeed, Japan has been Australia's single largest source of inbound visitors since 1990 when it eclipsed visitors from New Zealand. The number of Japanese overseas travellers peaked at 24% of Australia's total overseas visitors in 1992. In 1994, 720,937 Japanese visited Australia, in 1995 the numbers increased by 8.6% to 782,671 and rose a further 3.9% to 813,113 in 1996. In 1997, however, the growth rate slowed to only 0.1% with 813,892 Japanese visitors which then fell to 751,000 in 1998, a decrease of 7.7% on the previous year.¹⁵⁸ Nonetheless, this number accounted for 18% of all Australian inbound visitors, the largest group of tourists to Australia for that year.¹⁵⁹ In 1999, the number of Japanese visitors fell 6% on 1998 figures to represent 16% of all arrivals which allowed New Zealand to overtake Japan as the major source of overseas visitors to Australia.¹⁶⁰

6.140 Despite the significant drop in the number of Japanese visitors to Australia, overall tourist figures are holding up quite well. In 1999, 4,453,200 visitors arrived from overseas—a 7% increase on visitors from 1998.¹⁶¹ Numbers are being made up by European and American tourists.¹⁶²

6.141 According to the Australian Tourist Commission (ATC), Japan's total outbound tourism market is not expected to grow in the short term as Japan struggles with its current economic difficulties and its fragile consumer confidence. The most

156 Additional information supplied to the Committee by DFAT, 18 May 2000.

157 Australian Tourist Commission, submission no. 48, p. 1.

158 *Year Book 2000*, no. 82, p. 589; Australian Tourist Commission, submission no. 48, p. 1; Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 251; Junzo Yamaguchi, Japan Travel Bureau Australian Pty Ltd, *Committee Hansard*, 3 September 1999, p. 813.

159 Junzo Yamaguchi, Japan Travel Bureau, Australia Pty Ltd, *Committee Hansard*, 3 September 1999, p. 813.

160 Australian Bureau of Statistics, No. 3401.0—Overseas Arrivals and Departures, Australia, December 1999; Australian Tourist Commission, Short Term Overseas Visitor Arrivals, Year Ending December 1999, <http://www.atc.net.au/intell/data/99end.htm> (18 April 2000). In 1999, there were 707,463 short-term visitors from Japan and 728,798 from New Zealand.

161 Australian Bureau of Statistics, No. 3401.0—Overseas Arrivals and Departures, Australia, December 1999.

162 Karen Gilmour, DFAT, *Committee Hansard*, 15 February 1999, p. 34.

significant factor in the reduced levels of Japanese visitor arrivals is that almost 85% of Japanese short-term overseas travellers are holiday-makers and the Japanese share of this market is a substantial 29%. Most importantly, Japanese tourists spend more per day in Australia than any other overseas visitors. According to the BTR, Japanese visitors spend \$114 per day, while the average spent by other foreign tourists is \$80.¹⁶³

6.142 Thus the decrease in the number of Japanese tourists has serious implications for the Australian economy as this market has been a significant export earner for Australia, believed to be around \$3 billion per annum at the moment. This makes it one of Australia's key export items.¹⁶⁴

6.143 The decline in the number of Japanese travelling to Australia is reflected in the market for air travel, which has weakened in spite of the efforts to turn it around. Overall there has been a significant fall in total airline seats from Japan into Australia. Continued lack of profitability caused Qantas reluctantly to reduce services in November 1998 beyond the anticipated levels. The number of seats available dropped by 30% between 1998 and 1999. Overall the market in early 1999 was still falling and the Japan-Australia route continued to make a loss.¹⁶⁵

6.144 Not only are fewer Japanese visiting Australia but Australia's share of Japan's overseas tourist market has also dropped though only slightly. The ATC told the Committee that Australia's market share in 1997 was 4.84% and in 1998 it was 4.78% of all outbound travellers from Japan.

6.145 The economic downturn in Japan is of major and continuing concern to Australia's tourism industry. While the Japanese economy remains subdued and consumer confidence weak, potential Japanese travellers will defer their visits or look for cheaper short-haul destinations.¹⁶⁶ This trend is part of an overall pattern of spending in Japan where consumers are more careful with their money.¹⁶⁷

6.146 Australia has distinct advantages in attracting Japanese travellers to its shores. Its safe image and sites of educational value such as World Heritage listed areas and nature parks and a few major landmarks are the biggest attractions for Japanese tourists.¹⁶⁸ Australia continues to be the most preferred holiday destination for the

163 Junzo Yamaguchi, Japan Travel Bureau Australia Pty Ltd, *Committee Hansard*, 3 September 1999, p. 813.

164 Jeffrey Riethmuller, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 703.

165 Damien Wallace, Qantas Airways, *Committee Hansard*, 14 April 1999, pp. 233–6.

166 Australian Tourist Commission, submission no. 48, pp. 4–5.

167 Janet Tomi, DFAT, *Committee Hansard*, 15 February 1999, p. 8; Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 258.

168 Junzo Yamaguchi, Japan Travel Bureau Australia Pty Ltd, *Committee Hansard*, 3 September 1999, p. 815.

Japanese with research showing that potential Japanese travellers consistently rank Australia, given practical considerations of time and money, as the most favoured country for a holiday or for sight seeing. The ATC explained that Australia ranked 33% on this list of most preferred holiday destinations, a position held since 1990. The United States held second place at 28%, with Italy third at 20% and Hawaii fourth at 17%.¹⁶⁹ In summary, according to the Japan Foundation:

Australia is, for the Japanese, one of the countries they feel closest to. It is the country they most want to visit and trust the most. All of our surveys tell us that.¹⁷⁰

6.147 Unfortunately, Australia's high rating on paper does not translate into actual visitors. The challenge confronting the Australian tourist industry, especially in the face of Japan's economic worries, is to entice potential Japanese travellers to Australia.

6.148 One of the main tasks for the Australian tourist industry is to broaden and refresh Australia's image. Although Australia is perceived as a safe and relaxing place offering a wealth of outdoor activities; a country of sunshine, wide beaches and unspoilt natural wonders, the number of destinations attracting Japanese tourists is low. They come here to visit a limited number of attractions—the Opera House, the Sydney Harbour Bridge, Ayers Rock and the Great Barrier Reef. This lack of dispersion around Australia is a key characteristic of the Japanese tourist market over recent years.¹⁷¹

6.149 This narrow appreciation of Australia's attractions may account for the low level of repeat Japanese visitations. About 23% or 24% or a quarter of visitors from Japan to Australia have been here before. Although the reasons underpinning this low return rate are not fully clear, most Australians involved in the industry recognise it as a problem and believe it deserves closer attention.¹⁷² The ATC has recognised this as an important issue and believes:

...it is extremely important to give Japanese visitors a number of distinct reasons to want to return to Australia...One part of that is making sure that they are aware of a range of opportunities and a range of destinations within this country.

...

169 Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 250 and Australian Tourist Commission, submission no. 48, p. 4.

170 Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 51.

171 Australian Tourist Commission, submission no. 48, pp. 3–4.

172 Alan Loke, Qantas Airways, *Committee Hansard*, 14 April 1999, p. 247 and Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 254.

We therefore very strongly developed the view that we needed to introduce new destinations to the Japanese market. So what we have in place at the moment is a strategy called 'mono destination marketing' where we are trying to introduce new destinations to the market.¹⁷³

6.150 Clearly, Australia's image in Japan needs to be broadened.¹⁷⁴ The Japan Travel Bureau (JTB) also stressed the need to introduce new destinations situated away from Australia's eastern seaboard to Japanese travellers but accepted that one of the main problems is the cost of travel. Attractive destinations such as Tasmania have great potential to become popular with the Japanese market but the lack of direct flights from Japan makes airfares to these destinations very expensive.¹⁷⁵

6.151 The strongest disincentives for Japanese visitors include the time taken to reach Australia; the perceived number of tourists already here; and, importantly, the cost of the holiday.¹⁷⁶ According to the Japan Travel Bureau, the average person takes seven days holiday to come to Australia—the maximum they can visit is two cities.¹⁷⁷

6.152 The Australian Government has been working to develop the potential of the Japanese tourist market through a number of initiatives and in the 1998–99 budget provided an additional \$50 million over four years to the ATC to market and promote Australia as an overseas holiday destination. The government has also continued to develop Japan-Australia tourism relations through regular bilateral meetings at official level.¹⁷⁸

6.153 The ATC informed the Committee that it had launched the new 'Australia Time' promotional advertising campaign in October 1997. In its own words this campaign used 'a combination of humour and stunning footage to promote the revitalising effects of a holiday in Australia. The campaign spearheaded a range of integrated initiatives in brand advertising, publicity and other marketing activities.'

6.154 This campaign is continually being updated and modified. Most recently, it has been complemented by an additional focus on Western Australia with the active support and input of the Western Australian Tourist Commission.¹⁷⁹

173 Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 254.

174 See comments by Yoshihiro Tabe, Japan Local Government Centre, *Committee Hansard*, 14 April 1999, p. 285.

175 Junzo Yamaguchi, Japan Travel Bureau Australia Pty Ltd, *Committee Hansard*, 3 September 1999, pp. 814–15.

176 Australian Tourist Commission, submission no. 48, p. 4.

177 Junzo Yamaguchi, Japan Travel Bureau Australia Pty Ltd, *Committee Hansard*, 3 September 1999, p. 815.

178 Barry Jones, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 690.

179 Australian Tourist Commission, submission no. 48, pp. 2–3.

6.155 The ATC was also aware of the changing demographics in Japan and the importance to better target promotional campaigns to selected groups such as office ladies and the mature age or ‘silvers’ group which, because of the Japanese ageing population, is likely to assume increasing market importance.¹⁸⁰

6.156 Japanese student tourists are another group that offer substantial potential for Australia’s tourist industry. These young people, who visit Australia with school tours, are potential repeat visitors. As noted by the JTB, ‘The first experience of overseas travel is usually very impressive and encourages young people to revisit the country’. The ATC agrees with the JTB about the value of capturing the attention of young people ‘so they can experience at first hand some of the benefits of travel to Australia and then perhaps come down for their wedding and honeymoon and again as they move through to the “silvers”’. The ATC is keen to co-ordinate work being done in this area.¹⁸¹

6.157 While appreciating the ATC’s marketing programs, a number of witnesses felt that Australia needs to promote itself more effectively to the Japanese market—that their advertising products—especially their TV commercials—need to carry a more compelling message.¹⁸² The Japan Local Government Centre was more specific in submitting that Australia was not tapping the pool of potential Japanese travellers and needed to offer more familiarisation tours to the sales people over there.¹⁸³ Qantas is exploring the potential in this approach.¹⁸⁴

6.158 Australia cannot rely solely on its natural attributes to lure Japanese tourists; it must work hard to attract them. It is important to ensure that infrastructure and service delivery standards are high and meet the particular needs of visitor groups. Indeed establishing a reputation as a country that delivers a high quality tourist service might go some way to addressing the problem of the low return rate. A number of witnesses drew the Committee’s attention to specific issues that warrant serious consideration such as visa free travel; more efficient and quicker customs clearance; access by big

180 Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 257.

181 Junzo Yamaguchi, Japan Travel Bureau Australia Pty Ltd, *Committee Hansard*, 3 September 1999, p. 815 and see comments by Jeffrey Riethmuller, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 703.

182 Junzo Yamaguchi, Japan Travel Bureau Australia, Pty Ltd, *Committee Hansard*, 3 September 1999, p. 816.

183 Yoshihiro Tabe, Japan Local Government Centre, *Committee Hansard*, 14 April 1999, p. 286.

184 Damien Wallace, Qantas Airways, *Committee Hansard*, 14 April 1999, p. 233. Qantas told the Committee: ‘In 1998, it, in conjunction with Australian tourism interests, provided educational trips to Australia for over 1,000 Japanese travel agency staff and media representatives. Qantas will provide approximately 1,500 further educational visits for agents and media during calendar 1999. We believe that the provision of a hands-on look at the Australian product is a very valuable tool to put in the hands of those in a position to sway the consumer’s choice of destination.’

coaches to Sydney airport and parking facilities in the city.¹⁸⁵ Japanese returning from Australia could be the tourist industry's best advertisement.

6.159 The ATC wanted to restate its belief in the long-term importance of the Japanese market as a very strong and very significant source of visitor arrivals into Australia. It believed that the underlying popularity of Australia as a destination will continue, and is therefore very confident that in the longer term Japan will return to growth and continue its importance as a key source of arrivals into Australia.¹⁸⁶ Over the next 10 years, growth in visitor arrivals from Japan is expected to increase by an average of around 6% a year.¹⁸⁷

6.160 The Committee accepts that although there has been a fall in Japanese visitors coming to Australia, due in large measure to the economic downturn in Japan, the potential for growth in this market exists. It believes the time is ripe for the Australian tourist industry to look carefully at its overseas image and to use this downturn as an opportunity to refresh and rejuvenate Australia's overseas profile. It is also an opportunity to reassess and upgrade the infrastructure and the standard of delivery of tourist services.

6.161 The Committee believes that the recent slump in the number of Japanese visitors to Australia provides an ideal opportunity for the Australian tourist industry to reflect on their performance and on how they can improve it. They should seek to assess the quality of service delivery in the industry, the standard of facilities for overseas tourists, whether they meet visitor expectations and identify areas where Australia can deliver a better service. Areas mentioned by witnesses, such as visa requirements, customs clearance, coach access and parking facilities should only be the starting point of a more thorough and comprehensive assessment which should also look at travel costs and schedules and facilities, including hotels, guide services, shopping and reception.

Recommendation

The Committee recommends that the Australian Government commission a comprehensive study into the Australian tourist industry, using Japanese tourists as a case study and keeping in mind their low level of repeat visits, to ascertain how it can improve the standard of delivery of tourist services and broaden its overseas image.

185 Junzo Yamaguchi, Japan Travel Bureau Australia Pty Ltd, *Committee Hansard*, 3 September 1999, pp. 814–15;

186 Margaret Hudson, Australian Tourist Commission, *Committee Hansard*, 14 April 1999, p. 251.

187 Barry Jones, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 690.

Education

6.162 Education is an important export industry to Asia. Japan continues to be one of Australia's more important education export markets and was the sixth largest in 1998. The number of student visas issued to Japanese students onshore and offshore declined by 10% in 1998 to 9,400 due largely to the effect of the Asian financial and economic downturn.

6.163 According to the Department of Education, Training and Youth Affairs, there were about 10,800 Japanese students studying in Australia in 1998. This figure represents a decline of 9% from 1997. In addition, about 18,000 Japanese tourists enrolled in some form of study while visiting Australia in 1998. Japanese students studying in Australia on student visas generated an estimated revenue of about \$200 million in 1998. The Department told the Committee that preliminary estimates indicate that there will be some continuing decline in Japanese student enrolments but at a slower rate. It expected them to pick up in the medium to longer term.¹⁸⁸

6.164 The Department of Education is confident that Australia's image as a safe study destination, together with a growing awareness of the high quality of education available here, will help Australia win an increasing share of the Japanese education market in the medium to longer term.¹⁸⁹

6.165 Some witnesses, however, thought that Australian educational institutions had a challenging job ahead of them in drawing students to Australia's shores. According to Professor Yoshio Sugimoto, Australia is losing bright Japanese students to universities in the United States and Europe. He noted that many Australian universities have established institutional links in the exchange programs with Japan's universities and colleges, but they are mainly with second-class and third-rate institutions. Put bluntly, Australian universities have failed to attract top students from Japan—a situation that requires serious long-term planning.¹⁹⁰

6.166 Mr David Askew, a lecturer in Japanese studies, did agree with Professor Sugimoto that Australia was attracting students from second and third rate Japanese universities. He pointed out, however, that even if Japanese students coming to Australia were from lower rating universities they nonetheless would be 'wonderful sources of students for Australia'.¹⁹¹ The Committee agrees with this view but nonetheless is concerned about the overall low profile of Australian universities in Japan.

188 Robert Horne, Department of Education, Training and Youth Affairs, *Committee Hansard*, 28 May 1999, p. 707.

189 Robert Horne, Department of Education, Training and Youth Affairs, *Committee Hansard*, 28 May 1999, p. 707.

190 Professor Yoshio Sugimoto, *Committee Hansard*, 17 May 1999, pp. 520–1.

191 David Askew, *Committee Hansard*, 17 May 1999, p. 555.

6.167 In ranking universities, the Japanese student community does not place Australia at the top. The United States, with its commanding presence in mass media and in popular culture, and Europe, with its strong reputation and acknowledged tradition, are preferred to Australia. A young country, Australia has yet to establish a name in the international academic community. According to Professor Yoshio Sugimoto, Australian tertiary institutions have not campaigned sufficiently strongly in Japan where a lot of recruitment programs are in operation from various countries. Professor William Coaldrake, supported by a number of witnesses, stated that Australia needs to explore ways of attracting Japanese students to Australia.¹⁹²

6.168 Demographic changes in Japan will influence the demand for educational services. A falling birth rate in Japan means that there will be fewer young Japanese people seeking places in Australian educational institutions. However, even though families may be smaller, this does not mean that the family's investment in their children is insignificant. The education of children is still considered a priority in Japan and travel is an important aspect of education. Australia's proximity to Japan and favourable exchange rate mean that Australia will be a viable choice.¹⁹³

6.169 Given the recession, however, and the fall in consumer confidence, Japanese students are far more careful in spending on education. Expenditure on private education in Japan went down in a year by 18%. Overseas education is expensive and Japanese students may well choose less expensive options. Moreover, the sector of the market in which Australia is active—short courses for learning English—is vulnerable when consumer confidence is weak and people are looking to save not spend. The Department of Education suspects that the drop in overseas student numbers has been more pronounced for Australia than for the United States.¹⁹⁴

6.170 The low rate of economic growth in Japan and Australia's low profile in the academic world means that Australia will have to work hard to present itself as a worthy competitor to American and European institutions. Ms Rebecca Cross, Assistant Secretary, Australian Education International (AEI), stated:

What we are primarily trying to do is to raise the awareness of Australia as a study destination in the mind of potential students, because the first decision that a student makes when they are studying overseas is to choose the country. So to some extent we do need to raise awareness and we do market

192 Professor Yoshio Sugimoto, *Committee Hansard*, 17 May 1999, p. 525; Professor William Coaldrake, *Committee Hansard*, 17 May 1999, pp. 579–81; See also comments by Professor Alan Rix, *Committee Hansard*, 16 April 1999, pp. 452–3.

193 Dr Carolyn Stevens, *Committee Hansard*, 17 May 1999, p. 572.

194 Robert Horne, Department of Education, Training and Youth Affairs, *Committee Hansard*, 28 May 1999, pp. 707–8.

Australia as a high quality, safe environment and a good study destination.¹⁹⁵

6.171 AEI's marketing campaign—the Study in Australia 2000 campaign—carried this message about the quality of Australia's education system.¹⁹⁶ The biggest demand from Japan for education in Australia is to learn English, the so-called ELICOS (English Language Intensive Courses for Overseas Students), which accounts for two in every five Japanese students. The Committee found, however, that in this area, where Australia does have a presence and a great opportunity to showcase the high quality of Australian education and standards of service delivery, it is failing to promote itself as a provider of high quality education, indeed, it is creating a negative impression.

6.172 Professor Sugimoto told the Committee that he had heard Japanese language students studying in private language schools in Australia express dissatisfaction.¹⁹⁷ The Department of Education conceded that they receive 'criticisms occasionally from students who are disenchanted with the courses that they are being offered'. It went on to state:

Sometimes they will criticise the institution for low quality; and occasionally we have had criticisms or allegations the courses are not in fact even provided, that they are shopfront institutions.¹⁹⁸

6.173 The Committee realises that Australia has a challenge ahead in competing with established and world recognised educational institutions in attracting Japanese students. Nonetheless it has an opportunity to promote the reputation of Australia's education system and to encourage Japanese students to undertake further study in Australia through the ELICOS courses. Evidence suggests, however, that some of these courses are falling short in presenting a positive image of education in Australia. Clearly, this is an area that requires attention and calls for closer co-ordination between the state departments of education and the Federal Government.

195 Rebecca Cross, Department of Education, Training and Youth Affairs, *Committee Hansard*, 28 May 1999, p. 711.

196 Rebecca Cross, Department of Education, Training and Youth Affairs, *Committee Hansard*, 28 May 1999, p. 711.

197 Professor Yoshio Sugimoto, *Committee Hansard*, 17 May 1999, p. 525. He told the Committee that 'anecdotal evidence suggests that some private language institutions are not providing good quality education because of the relatively poor quality of teachers'.

198 Sara Cowan, Department of Education, Training and Youth Affairs, *Committee Hansard*, 28 May 1999, p. 709.

Recommendation

The Committee recommends that the Australian Government confer with State Governments to ensure that educational institutions offering ELICOS (English Language Intensive Courses for Overseas Students) maintain high standards in education and the service they deliver to overseas students.

